

RENHENG ENTERPRISE HOLDINGS LIMITED

仁恒實業控股有限公司

(Incorporated in the Cayman Islands with limited liability)

Stock Code: 8012



PLACING

Sponsor and Lead Manager



Shenyin Wanguo Capital (H.K.) Limited

IMPORTANT

If you are in any doubt about any of the contents of this prospectus, you should obtain independent professional advice.



RENHENG Enterprise Holdings Limited
仁恒實業控股有限公司

RENHENG ENTERPRISE HOLDINGS LIMITED 仁恒實業控股有限公司

(Incorporated in the Cayman Islands with limited liability)

LISTING ON THE GROWTH ENTERPRISE MARKET OF THE STOCK EXCHANGE OF HONG KONG LIMITED BY WAY OF PLACING OF SHARES

Number of Placing Shares : 50,000,000 Placing Shares
Placing Price : Not more than HK\$1.30 per Share and expected to be not less than HK\$1.10 per Share (plus brokerage of 1%, SFC transaction levy of 0.003% and Stock Exchange trading fee of 0.005% payable in full on application in Hong Kong dollars)
Nominal value : HK\$0.01 each
Stock code : 8012

Sponsor and Lead Manager



Shenyin Wanguo Capital (H.K.) Limited

Hong Kong Exchanges and Clearing Limited, The Stock Exchange of Hong Kong Limited and Hong Kong Securities Clearing Company Limited take no responsibility for the contents of this prospectus, make no representation as to its accuracy or completeness and expressly disclaim any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this prospectus.

A copy of this prospectus, having attached thereto the documents specified in the paragraph headed "Documents delivered to the Registrar of Companies" in Appendix VI to this prospectus, has been registered by the Registrar of Companies in Hong Kong as required by section 342C of the Companies Ordinance. The Securities and Futures Commission and the Registrar of Companies in Hong Kong take no responsibility as to the contents of this prospectus or any other documents referred to above. Prior to making an investment decision, prospective investors should carefully consider all the information set out in this prospectus, including the risk factors set out in the section headed "Risk factors" in this prospectus.

The Placing Price is expected to be fixed between Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) and the Company on or before the Price Determination Date, which is currently scheduled on 9 November 2011 (or such later date as agreed between the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter)). The Placing Price will not be more than HK\$1.30 per Share and is currently expected to be not less than HK\$1.10 per Share unless otherwise announced. The indicative Placing Price range may be reduced below that stated in this prospectus at any time on or before the Price Determination Date. In such a case, the Company will, as soon as practicable following the decision to make such reduction, cause to be published on the GEM website at www.hkgem.com and our Company's website at www.renhengenterprise.com an announcement of such change on or before the Price Determination date.

If Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) and the Company are unable to reach any agreement on the Placing Price by the Price Determination Date or such later date as agreed by the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter), the Placing will not become unconditional and will not proceed. In such event, the Company will issue an announcement on the GEM website at www.hkgem.com and the Company's website at www.renhengenterprise.com.

Prospective investors of the Placing Shares should note that Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter), is entitled to terminate the Underwriting Agreement by giving notice in writing to the Company upon the occurrence of any of the events set forth under the sub-paragraph headed "Grounds for termination" under the paragraph headed "Underwriting arrangements" in the section headed "Underwriting" in this prospectus at any time prior to 8:00 a.m. (Hong Kong time) on the Listing Date.

CHARACTERISTICS OF GEM

GEM has been positioned as a market designed to accommodate companies to which a higher investment risk may be attached than other companies listed on the Stock Exchange. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.

Given the emerging nature of companies listed on GEM, there is a risk that securities traded on GEM may be more susceptible to high market volatility than securities traded on the Main Board and no assurance is given that there will be a liquid market in the securities traded on GEM.

EXPECTED TIMETABLE

2011
(Note 1)

Price determination on (Note 2)	Wednesday, 9 November
Announcement of the Placing Price and the level of indication of interest in the Placing to be published on the GEM website at www.hkgem.com and the Company's website at www.renhengenterprise.com on or before	Thursday, 17 November
Allotment of Placing Shares to places on or before	Thursday, 17 November
Deposit of share certificates for the Placing Shares into CCASS on or before (Note 3)	Thursday, 17 November
Dealings in Shares on GEM to commence at	9:00 a.m. on Friday, 18 November

Notes:

1. All times and dates refer to Hong Kong times and dates, except as otherwise stated.
2. The Price Determination Date is expected to be on Wednesday, 9 November 2011. If the Placing Price is not agreed on that date, or such later date as agreed by the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter), the Placing will not become unconditional and will not proceed.
3. The share certificates for the Placing Shares to be distributed via CCASS are expected to be deposited into CCASS on or before Thursday, 17 November 2011 for credit to the relevant CCASS Participants' stock accounts designated by the Underwriter, the places or their respective agents (as the case may be). No temporary documents or evidence of title will be issued.
4. All share certificates will only become valid certificates of title when the Placing has become unconditional in all respects and the Underwriting Agreement has not been terminated in accordance with its terms prior to 8:00 am. (Hong Kong time) on the Listing Date.

If there is any change in the above expected timetable, the Company will issue a separate announcement.

For details of the structure of the Placing, including conditions thereof, please refer to the sections headed "Information about this prospectus and the Placing" and "Structure and conditions of the Placing" in this prospectus.

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You should rely only on the information contained in this prospectus to make your investment decision.

The Company, the Sponsor and the Underwriter have not authorised anyone to provide you with information that is different from what is contained in this prospectus.

Any information or representation not made nor contained in this prospectus must not be relied on by you as having been authorised by the Company, the Sponsor, the Underwriter, any of their respective directors, officers, employees, advisers, agents, representatives or affiliates of any of them or any other persons or parties involved in the Placing.

The contents of the Company's website at www.renhengenterprise.com do not form part of this prospectus.

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SUMMARY

This summary aims to give you an overview of the information contained in this prospectus. As this is a summary, it does not contain all the information that may be important to you. You should read this prospectus in its entirety before you decide to invest in the Placing Shares.

The information in respect of the market position or the market share of our Group is not presented in this prospectus as no official statistics of the tobacco machinery market is available from the relevant government authorities, industry bodies, research agencies and/or other reliable public domain.

There are risks associated with any investment. Some of the particular risks in investing in the Placing Shares are set out in the section headed "Risk factors" in this prospectus. You should read that section carefully before you decide to invest in the Placing Shares.

OVERVIEW

We are principally engaged in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of tobacco machinery products in the PRC. We generate our turnover primarily from projects related to three types of catalogued special-purpose tobacco machinery products as listed on the Tobacco Machinery Documents, namely casing and flavouring systems, pneumatic feeding systems (PF systems) and pre-pressing packing machines (PP systems), and related components and devices not listed on all of the Tobacco Machinery Documents, which accounted for approximately 92.6%, 95.4% and 93.0% of our turnover for each of the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively.

Catalogued special-purpose tobacco machinery products as listed in the Tobacco Machinery Documents and components and/or devices which are not listed in the Tobacco Machinery Documents

In providing our catalogued special-purpose tobacco machinery products as listed in all of the Tobacco Machinery Documents, we enter into contracts directly with CTMC. Furthermore, in order to meet the functional specification of our end customers, we may also contract with end customers directly to supply components and/or devices which are not listed in all of the Tobacco Machinery Documents but form integral parts of the customised systems. These components and devices included, but were not limited to, conveyer structures, automated filling devices, automated dosing devices, filling valves, control units of blending, filling and rinsing, and mechanical items such as stirrers and drive dogs equipped with the customised casing and flavouring system with movable tanks. Please refer to the paragraph headed "Business model" under the section headed "Business" in this prospectus for a description of the functions of these components and devices. The types of components and devices may vary depending on the specifications and design requirements of our end customers. Having considered that these components and devices (i) are not standalone systems as defined in the Tobacco Machinery List; and (ii) are not listed in the Pricing Guidelines or Pricing Approval 2010, the PRC Legal Advisers are of the opinion that those components and devices should not be classified as catalogued special-purpose tobacco machinery and the requirements pursuant to the Measures on Administration of Procurement are not applicable to the sales of these items, and hence such transactions with our end customers during the Track Record Period were not in breach of the relevant PRC laws and regulations.

SUMMARY

Tobacco Production Licence

Under the relevant PRC regulations, domestic manufacturers engaging in the production of tobacco machinery as listed on the Tobacco Machinery List must possess the Tobacco Production Licence to manufacture and sell the relevant tobacco machinery. The Tobacco Machinery List sets out 22 types of catalogued special-purpose tobacco machinery deployed in the production of tobacco products in the PRC and the Pricing Guidelines specify the guidance price of different models of catalogued special-purpose tobacco machinery products, whereas the Pricing Approval 2010 sets out the guidance price of various models of casing and flavouring systems not specified in the Pricing Guidelines. We have obtained a Tobacco Production Licence under which we are permitted to manufacture, sell and provide maintenance, overhaul as well as modification services in respect of casing and flavouring systems, feeding systems and PP systems. Our current licence is valid for a period of five years commenced from 14 April 2009 and will expire on 14 April 2014. According to the China Tobacco Year Book 2009 published by STMA in December 2010, as at the end of 2009, there were 34 tobacco machinery manufacturers which have been granted the Tobacco Production Licence for the manufacture and sale of various types of catalogued special-purpose tobacco machinery.

Non-catalogued ancillary tobacco machinery products and services

We are also engaged in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of non-catalogued ancillary tobacco machinery products and services, which mainly include dedusting systems and swelling agent delivery systems. According to the PRC Legal Advisers, the sale of non-catalogued ancillary tobacco machinery products is not subject to the requirements under the Measures on Administration of Procurement as such products are not listed in all of the Tobacco Machinery Documents. Accordingly, manufacturers are not required to obtain the Tobacco Production Licence or other licences from STMA or local tobacco monopoly authorities to sell non-catalogued ancillary tobacco machinery products.

Turnover for the six months ended 30 June 2011

Our turnover increased by approximately 153.2% or HK\$39,113,000 from approximately HK\$25,538,000 for the six months ended 30 June 2010 to approximately HK\$64,651,000 for the six months ended 30 June 2011. The increase was mainly attributable to substantial turnover recognised from our customised casing and flavouring system with movable tanks to a cigarette manufacturer in Kunming for the six months ended 30 June 2011, which had an aggregate contract value of approximately RMB79,238,000. Turnover derived from our casing and flavouring systems increased by approximately 223.2% or HK\$39,623,000 from approximately HK\$17,751,000 for the six months ended 30 June 2010 to approximately HK\$57,374,000 for the six months ended 30 June 2011, which was primarily attributable to recognition of turnover of approximately HK\$51,369,000 from our customised casing and flavouring system project for the cigarette manufacturer in Kunming as mentioned above.

Gross profit margin for the six months ended 30 June 2011

Our gross profit margin for the six months ended 30 June 2011 decreased to 32.3% as compared to the gross profit margin of 38.1% for the corresponding period in 2010 and 44.3% for the year ended 31 December 2010. The decrease in our gross profit margin in the first half of 2011 was mainly

SUMMARY

attributable to the decrease in turnover from our PF systems and PP systems which generated higher gross profit margins than our casing and flavouring systems and the decrease in gross profit margin of our casing and flavouring system. The gross profit margin of casing and flavouring systems was 30.2% for the six months ended 30 June 2011, which was higher than that of 26.9% for the corresponding period in 2010 but was lower than that of 36.6% for the year ended 31 December 2010. The decrease in our gross profit margin in the first half of 2011 as compared to the full year of 2010 was mainly attributable to the project contracted in April 2010 with an aggregate contract value of approximately RMB79,238,000, in which we contracted to supply a customised casing and flavouring system with movable tanks for a cigarette manufacturer in Kunming. As this customised casing and flavouring system with movable tanks was the first of its kind that we built and its technical viability could not be foreseen with certainty, our Group has accepted a low mark up relative to the expected costs in respect of the components and devices when deciding the aggregate contract amount charged to the end customer based on mutual agreement, resulting in a lower gross profit margin for this project and thus the lower gross profit margin for our casing and flavouring systems for the period.

During the six months ended 30 June 2011, the gross profit margin for the sales of parts and sales of components and devices which were not listed in all of the Tobacco Machinery Documents and were not contracted with CTMC but form integral parts of the customised systems was approximately 24.9%, whilst the gross profit margin for the sales of components and devices in respect of the customised casing and flavouring system with movable tanks for a cigarette manufacturer in Kunming was approximately 22.3%.

Net profit margin for the six months ended 30 June 2011

Our net profit margin decreased from approximately 13.4% for the six months ended 30 June 2010 to approximately 5.6% for the six months ended 30 June 2011, which was in line with the decrease in gross profit margin as discussed above, the recognition of listing expenses as well as the increase in our effective tax rate from 30.6% for the six months ended 30 June 2010 to 46.2% for the six months ended 30 June 2011 due primarily to the recognition of the listing expenses which are not deductible for tax purpose.

Contracts signed but not completed as at 31 August 2011

The aggregate value of contracts signed with our customers as of 31 August 2011 less revenues recognised in connection with such contracts up to and including the same date amounted to approximately RMB134,788,000. For further details, please refer to the paragraph headed “Products and services – Contracts signed but not completed as at 31 August 2011” under the “Business” section in this prospectus.

Our business model

We conduct our tobacco machinery product business on a project basis and all of our products are custom-made to meet the needs of our customers in the PRC.

SUMMARY

Pursuant to the Measures on Administration of Procurement, procurements of catalogued special-purpose tobacco machinery listed on the Tobacco Machinery List must be approved by STMA in advance. In addition, pursuant to these regulations, CTMC, being a subsidiary unit of CNTC, monitors and oversees all domestic made catalogued special-purpose tobacco machinery procurement matters between the tobacco machinery manufacturers and the cigarette manufacturers in the PRC. CTMC acts as a government agency to fulfill the relevant regulatory requirements in the procurement arrangements and is not involved in the negotiations regarding the transactions which are carried out between the tobacco machinery manufacturers and the purchasers. CTMC enters into sale and purchase agreements with the tobacco machinery manufacturers in connection with the machinery procurements made by cigarette manufacturers. We deliver our catalogued special-purpose machinery products directly to the cigarette manufacturers and tobacco redrying factories. By virtue of our contractual relationship with CTMC under the aforesaid regulatory requirements in respect of catalogued special-purpose tobacco machinery procurement arrangements, CTMC was our largest customer during the two years ended 31 December 2010 and was our second largest customer for the six months ended 30 June 2011 and accounted for approximately 73.3%, 66.1% and 33.9% of our turnover for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. Nevertheless, the end customers of our catalogued special-purpose tobacco machinery are normally cigarette manufacturers (in the case of our casing and flavouring systems and PF systems) and tobacco redrying factories (in the case of our PP systems).

We follow the guidance price as specified in the Pricing Guidelines and Pricing Approval 2010 issued by STMA in pricing our catalogued special-purpose tobacco machinery products. However, in the event that the guidance price in the Pricing Guidelines or the Pricing Approval 2010 of a specific catalogued product proves to be commercially unacceptable to follow, we can file an application to STMA requesting for a revision of the guidance price. Applications for the revision of the guidance prices as specified in the Pricing Guidelines and Pricing Approval 2010 can be made to 國家煙草專賣局發展計劃司 (the development and planning division of STMA) and CTMC. However, as at the Latest Practicable Date, no regulations or guidelines had been issued by STMA on the revision of the guidance prices for tobacco machinery. During the Track Record Period and up to the Latest Practicable Date, we did not file any application for the revision of the guidance price and had not received any notice in respect of the revision of the guidance prices as specified in the Pricing Guidelines or the Pricing Approval 2010.

In providing (i) components and devices related to our catalogued special-purpose tobacco machinery which are not listed in all of the Tobacco Machinery Documents; (ii) our other non-catalogued ancillary tobacco machinery products; and (iii) maintenance, overhaul and modification services in respect of our tobacco machinery products, we enter into contracts directly with the end customers.

The tobacco industry in the PRC is highly regulated. STMA and CNTC are responsible for the centralised management of the industry. We have seen the average per capita consumption expenditure in tobacco-related products by urban residents in the PRC grew at a CAGR of approximately 11.3% from 2004 to 2009, whilst the fixed asset investment in relation to equipment purchasing in the tobacco product industry in urban areas amounted to approximately RMB10.0 billion in 2009. Our Directors believe that, with its competitive strengths, our Group is well positioned to capture the growing business opportunities in the tobacco machinery market in the PRC.

SUMMARY

Turnover breakdown by project category

Our turnover of catalogued special-purpose tobacco machinery projects includes that derived from sales of three types of catalogued special-purpose tobacco machinery products and parts as well as sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents and are not contracted with CTMC but form integral parts of the customised systems. The following table sets forth a breakdown of our turnover by project category during the Track Record Period:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Catalogued special-purpose tobacco machinery projects								
Sales of tobacco machinery and parts/components/devices (<i>Note i</i>)								
Casing and flavouring systems	37,873	52.2	48,097	52.5	16,982	66.5	55,237	85.4
PF systems	10,545	14.5	13,790	15.0	5,215	20.4	936	1.5
PP systems	4,858	6.7	2,381	2.6	–	–	–	–
	<u>53,276</u>	<u>73.4</u>	<u>64,268</u>	<u>70.1</u>	<u>22,197</u>	<u>86.9</u>	<u>56,173</u>	<u>86.9</u>
Provision of maintenance, overhaul and modification services								
Casing and flavouring systems	11,288	15.5	13,091	14.3	769	3.0	2,137	3.3
PF systems	1,854	2.6	4,015	4.4	1,192	4.7	1,540	2.4
PP systems	805	1.1	6,095	6.6	510	2.0	273	0.4
	<u>13,947</u>	<u>19.2</u>	<u>23,201</u>	<u>25.3</u>	<u>2,471</u>	<u>9.7</u>	<u>3,950</u>	<u>6.1</u>
Sub-total								
Casing and flavouring systems	49,161	67.7	61,188	66.8	17,751	69.5	57,374	88.7
PF systems	12,399	17.1	17,805	19.4	6,407	25.1	2,476	3.9
PP systems	5,663	7.8	8,476	9.2	510	2.0	273	0.4
	<u>67,223</u>	<u>92.6</u>	<u>87,469</u>	<u>95.4</u>	<u>24,668</u>	<u>96.6</u>	<u>60,123</u>	<u>93.0</u>
Other projects and products								
Sales of non-catalogued ancillary tobacco machinery (<i>Note ii</i>)								
Provision of maintenance, overhaul and modification services	3,757	5.2	498	0.5	870	3.4	–	–
Sales of hot stamped foil products	–	–	1,621	1.8	–	–	2,242	3.5
	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Sub-total								
	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Total								
	<u>72,616</u>	<u>100.0</u>	<u>91,713</u>	<u>100.0</u>	<u>25,538</u>	<u>100.0</u>	<u>64,651</u>	<u>100.0</u>

SUMMARY

- Notes:* (i) Turnover of catalogued special-purpose tobacco machinery projects contracted with CTMC amounted to approximately HK\$53,208,000, HK\$60,589,000 and HK\$21,893,000 respectively, representing approximately 73.3%, 66.1% and 33.9% of our total turnover respectively during the Track Record Period. Turnover generated from catalogued special-purpose tobacco machinery projects also includes that derived from sales of parts and sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents and are not contracted with CTMC but form integral parts of the customised systems, which amounted to approximately HK\$68,000, HK\$3,679,000 and HK\$34,280,000 respectively, representing 0.1%, 4.0% and 53.0% of our total turnover respectively during the Track Record Period. Despite the separate sale and purchase agreements, as these components and/or devices were included in the technical specification of the corresponding catalogued special-purpose tobacco machinery projects and cannot function separately from the catalogued special-purpose tobacco machinery system, the revenue derived from the sales of these items is classified under the relevant category of catalogued special-purpose tobacco machinery projects.
- (ii) Non-catalogued ancillary tobacco machinery products mainly comprised dedusting systems and swelling agent delivery systems.

Our largest customers during the Track Record Period

By virtue of our contractual relationship with CTMC under the Measures on Administration of Procurement in respect of catalogued special-purpose tobacco machinery procurement arrangements, CTMC was our largest customer during the two years ended 31 December 2010 and the second largest customer for the six months ended 30 June 2011 and accounted for approximately 73.3%, 66.1% and 33.9% of our turnover for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. Nevertheless, the end customers of our catalogued special-purpose tobacco machinery are generally cigarette manufacturers (in the case of our casing and flavouring systems and PF systems) and tobacco redrying factories (in the case of our PP systems).

For the six months ended 30 June 2011, our largest customer was a cigarette manufacturer based in Kunming, Yunnan, the PRC. Turnover derived from this customer for the six months ended 30 June 2011 mainly comprised the substantial turnover recognised from the customised casing and flavouring system with movable tanks project with this customer. As the first of its kind system built by our Group, which was of larger scale and higher degree of complexity, the customisation of the said casing and flavouring system required the installation of certain components and devices sourced at higher costs to meet our customer's specifications. As these components and devices were not included in the Tobacco Machinery Documents, their sales were not required to be contracted with CTMC. We contracted directly with this customer, thus leading to a high turnover attributable to this customer and relatively lower turnover attributable to CTMC during the period.

Our turnover generated from construction contracts of casing and flavouring systems is recognised using the percentage of completion method by reference to the value of work carried out during the year/period as determined by progress verification certificate. Turnover from all other products represents gross invoiced sales, net of discounts and value-added tax. The following sets out the breakdown of our turnover by customer group during the Track Record Period.

SUMMARY

	Year ended 31 December				Six months ended 30 June			
	2009	2010	2010	2011	2010	2011	2010	2011
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Catalogued special-purpose tobacco machinery projects								
Casing and flavouring systems								
Sales of tobacco machinery to CTMC	37,805	52.1	46,129	50.3	16,982	66.5	20,957	32.4
Sales of tobacco machinery to other customers	68	0.1	1,968	2.2	–	–	34,280	53.0
Provision of maintenance, overhaul and modification services to other customers	11,288	15.5	13,091	14.3	769	3.0	2,137	3.3
	<u>49,161</u>	<u>67.7</u>	<u>61,188</u>	<u>66.8</u>	<u>17,751</u>	<u>69.5</u>	<u>57,374</u>	<u>88.7</u>
PF systems								
Sales of tobacco machinery to CTMC	10,545	14.5	12,079	13.2	5,215	20.4	936	1.5
Sales of tobacco machinery to other customers	–	–	1,711	1.8	–	–	–	–
Provision of maintenance, overhaul and modification services to other customers	1,854	2.6	4,015	4.4	1,192	4.7	1,540	2.4
	<u>12,399</u>	<u>17.1</u>	<u>17,805</u>	<u>19.4</u>	<u>6,407</u>	<u>25.1</u>	<u>2,476</u>	<u>3.9</u>
PP systems								
Sales of tobacco machinery to CTMC	4,858	6.7	2,381	2.6	–	–	–	–
Sales of tobacco machinery to other customers	–	–	–	–	–	–	–	–
Provision of maintenance, overhaul and modification services to other customers	805	1.1	6,095	6.6	510	2.0	273	0.4
	<u>5,663</u>	<u>7.8</u>	<u>8,476</u>	<u>9.2</u>	<u>510</u>	<u>2.0</u>	<u>273</u>	<u>0.4</u>
Sub-total	<u>67,223</u>	<u>92.6</u>	<u>87,469</u>	<u>95.4</u>	<u>24,668</u>	<u>96.6</u>	<u>60,123</u>	<u>93.0</u>
Other projects and products								
Sales of tobacco machinery to other customers	1,636	2.2	2,125	2.3	–	–	2,286	3.5
Provision of maintenance, overhaul and modification services to other customers	3,757	5.2	498	0.5	870	3.4	–	–
Sales of hot stamped foil products	–	–	1,621	1.8	–	–	2,242	3.5
Sub-total	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Total	<u>72,616</u>	<u>100.0</u>	<u>91,713</u>	<u>100.0</u>	<u>25,538</u>	<u>100.0</u>	<u>64,651</u>	<u>100.0</u>

SUMMARY

Net operating cash outflow and total net cash outflow for the six months ended 30 June 2011

We incurred net operating cash outflow of approximately HK\$12,005,000 and total net cash outflow of approximately HK\$15,804,000 for the six months ended 30 June 2011. Our business is project based and the time needed for completing our projects may vary from 1 month to 9 months depending on the size of our projects. In respect of our tobacco machinery projects, we typically would receive an initial payment ranging from 10% to 30% of the contract value from our customers upon signing the contract and would receive the majority of the payment from our customers upon completion of the project. Therefore, we may have to pay in advance certain costs and expenses in relation to some of the contracts prior to receiving adequate funds to cover such costs and expenses. The net operating cash outflow and total net cash outflow for the six months ended 30 June 2011 were mainly attributable to the increase in inventories and amounts due from customers for contract work and decrease in amount due to a customer for contract work in relation to our projects in progress. The increase in amounts due from customers for contract work during the first half of 2011 was mainly due to the contract costs incurred from the customised casing and flavouring system with movable tanks project in progress in Kunming exceeded the corresponding progress billings charged to our customer up to 30 June 2011. We expect the progress billings in relation to this project will be charged to our customer in November 2011. Meanwhile the decrease in amount due to a customer for contract work during the six months ended 30 June 2011 was due to the subsequent contract costs incurred plus recognised profits setting off the progress billing previously charged to this customer in 2010 in relation to the casing and flavouring system with movable tanks project in Kunming. During the period, we also incurred listing expenses of approximately HK\$2,225,000 and paid PRC enterprise income tax of approximately HK\$7,790,000. Notwithstanding that, we did not incur net operating cash outflow for the years ended 31 December 2009 and 31 December 2010.

As our Group did not have any borrowings, mortgages or charges, or material contingent liabilities outstanding as at 31 August 2011, and we had bank balances and cash of approximately HK\$40,012,000 and HK\$30,801,000 as at 30 June 2011 and 31 August 2011 respectively, while the progress billing in respect of the aforementioned casing and flavouring system is expected to be charged to the customer in November 2011, our Directors are of the view that the net operating cash outflow and overall net cash outflow for the six months ended 30 June 2011 are not likely to have any material adverse impact on our operations.

COMPETITIVE STRENGTHS

We believe we have the following competitive strengths:

- Well established and proven development and customisation capabilities
- Commitment to product quality
- Long standing relationships with cigarette manufacturers and tobacco redrying factories
- Experienced management team

SUMMARY

BUSINESS OBJECTIVE AND STRATEGIES

Our Group aims to leverage on our competitive strengths and strive to become one of the leading tobacco machinery manufacturers in the PRC. To achieve our business objective, we intend to adopt the following principal strategies:

- Continuous product development and innovation
- Enhancing corporate profile and increasing market penetration
- Enhancing production processing capabilities
- Strengthening management information system

SUMMARY HISTORICAL CONSOLIDATED FINANCIAL INFORMATION

You should read the summary historical consolidated financial information set forth below in conjunction with our consolidated financial statements included in the Accountants' Report set forth in Appendix I to this prospectus, which are prepared in accordance with HKFRS, together with the accompanying notes thereto. Operating results in any historical period may not be indicative of the results that may be expected in any future period.

SUMMARY

Consolidated statements of comprehensive income

	Year ended 31 December		Six months ended 30 June	
	2009	2010	2010	2011
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
			(unaudited)	
Turnover	72,616	91,713	25,538	64,651
Cost of sales	<u>(44,195)</u>	<u>(51,099)</u>	<u>(15,800)</u>	<u>(43,776)</u>
Gross profit	28,421	40,614	9,738	20,875
Other income	3,877	4,279	2,154	1,038
Other gains and losses	34	713	510	(14)
Selling and distribution costs	(9,064)	(8,817)	(4,189)	(6,985)
Administrative expenses	(6,182)	(7,456)	(3,267)	(5,963)
Listing expenses	–	(1,595)	–	(2,225)
Interest on bank loans wholly repayable within five years	<u>(353)</u>	<u>–</u>	<u>–</u>	<u>–</u>
Profit before taxation	16,733	27,738	4,946	6,726
Taxation	<u>(5,748)</u>	<u>(7,805)</u>	<u>(1,512)</u>	<u>(3,108)</u>
Profit for the year/period	10,985	19,933	3,434	3,618
Other comprehensive income:				
Exchange differences arising on translation	<u>592</u>	<u>2,775</u>	<u>622</u>	<u>2,235</u>
Total comprehensive income for the year/period	<u><u>11,577</u></u>	<u><u>22,708</u></u>	<u><u>4,056</u></u>	<u><u>5,853</u></u>

SUMMARY

Consolidated statements of financial position

	As at 31 December		As at
	2009	2010	30 June
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Non-current assets			
Property, plant and equipment	14,261	14,664	15,197
Land use rights	2,972	3,002	3,035
Investment properties	16,930	18,305	18,999
	<u>34,163</u>	<u>35,971</u>	<u>37,231</u>
Current assets			
Inventories	21,851	17,928	22,112
Trade and other receivables	21,440	42,503	46,511
Land use rights	68	71	72
Amounts due from customers			
for contract work	3,908	1,614	23,947
Amount due from ultimate holding company	388	–	–
Amounts due from related companies	7,056	417	427
Restricted bank deposit	–	237	243
Bank balances and cash	5,629	54,383	40,012
	<u>60,340</u>	<u>117,153</u>	<u>133,324</u>
Current liabilities			
Trade and other payables	18,029	41,450	68,155
Amount due to a customer for contract work	–	8,061	–
Amounts due to related companies	519	2,500	–
Tax payable	3,788	5,959	1,957
	<u>22,336</u>	<u>57,970</u>	<u>70,112</u>
Net current assets	<u>38,004</u>	<u>59,183</u>	<u>63,212</u>
Total assets less current liabilities	72,167	95,154	100,443
Non-current liabilities			
Deferred tax liabilities	794	1,073	509
	<u>71,373</u>	<u>94,081</u>	<u>99,934</u>
Capital and reserves			
Share capital	390	390	–
Reserves	70,983	93,691	99,934
Total equity	<u>71,373</u>	<u>94,081</u>	<u>99,934</u>

SUMMARY

USE OF PROCEEDS

The net proceeds from the Placing based on the Placing Price of HK\$1.20 per Share (being the mid-point of the stated range of the Placing Price), after deducting the underwriting fees and other expenses, are estimated to be approximately HK\$47.3 million. Our Directors intend to apply the aforesaid net proceeds in the following manner:

	From the Latest Practicable Date to		For the six months ending			Total
	31 December 2011	30 June 2012	31 December 2012	30 June 2013	31 December 2013	
	(HK\$'000)	(HK\$'000)	(HK\$'000)	(HK\$'000)	(HK\$'000)	
Continuous product development and innovation	1,364	5,694	9,542	13,353	3,760	33,713
Enhancing corporate profile and increasing market penetration	18	156	1,276	1,040	1,210	3,700
Enhancing production processing capabilities	480	960	1,500	670	1,220	4,830
Strengthening management information system	480	-	-	-	-	480
	<u>2,342</u>	<u>6,810</u>	<u>12,318</u>	<u>15,063</u>	<u>6,190</u>	<u>42,723</u>

The balance of approximately HK\$4.6 million will be applied towards additional general working capital of our Group.

During the Track Record Period, our total product research and development expenditures amounted to approximately HK\$246,000, HK\$394,000 and HK\$717,000 respectively, which represented approximately 0.3%, 0.4% and 1.1% respectively of our total turnover. We believe that the users of our products, being mainly cigarette manufacturers in the PRC, are focused on continuous technological improvements in their cigarette production process. As a result, in order to maintain our competitiveness, our Directors intend to apply approximately 71.2% of the above net proceeds on continuous product development and innovation, despite the small amounts of product research and development expenditures recorded during the Track Record Period. We plan to expand our product range and create new and enhanced series of catalogued special-purpose tobacco machinery products with innovative designs to meet the evolving requirements of cigarette manufacturers and tobacco redrying factories. We also intend to expand our scope of catalogued special-purpose tobacco machinery products and launch two research and development programs related to the development of (i) tobacco bale slicer designed for use by the cigarette manufacturers in slicing unwrapped tobacco bale into slices of required sizes

SUMMARY

for subsequent tobacco processing; and (ii) tobacco redrying system designed for use by tobacco redrying factories in the redrying process. We intend to use the above net proceeds from the Placing of HK\$33,713,000 on continuous product development and innovation as follows:

- approximately HK\$10,883,000 for designing and producing prototypes of a new casing and flavouring system equipping the operating features of movable tanks and automated storage, retrieval and feeding devices comprising the costs of materials, parts, components and toolings;
- approximately HK\$4,340,000 for designing and producing prototypes of a new type of spraying device comprising the costs of materials, parts, components and toolings;
- approximately HK\$4,500,000 for developing and producing prototypes of a new set of PP system employing two compressors comprising the costs of materials, parts, components and toolings;
- approximately HK\$680,000 for developing and producing prototypes of a new set of PF system with only one tube connecting to one cigarette wrapping machine and with a higher delivery capacity as compared to the existing system;
- approximately HK\$4,780,000 and HK\$7,230,000 for developing and producing prototypes of tobacco bale slicer and tobacco redrying system respectively comprising the costs of materials, parts, components and toolings; and
- approximately HK\$1,300,000 for recruiting additional technical staff for project design and product development.

Apart from applying the net proceeds from the Placing of approximately HK\$4,830,000 on the purchase of machinery and equipment to enhance our production processing capabilities, details of which are disclosed in the paragraph headed “Implementation plans – 3. Enhancing production processing capabilities” in the section headed “Future plans and prospects” in this prospectus, our Directors do not plan to use the net proceeds on capital expenditures for continuous product development and innovation.

Our Directors consider that the net proceeds from the Placing of approximately HK\$47.3 million will be sufficient to finance our Group’s business plans up to the year ending 31 December 2013.

To the extent that the net proceeds from the issue of the Placing Shares are not immediately required for the above purpose, it is the present intention of our Directors that such proceeds will be placed on short-term interest bearing deposits with authorised financial institutions.

SUMMARY

OFFERING STATISTICS⁽¹⁾

	Based on the Placing Price of HK\$1.10 per Share	Based on the Placing Price of HK\$1.30 per Share
Market capitalisation of our Shares ⁽²⁾	HK\$220 million	HK\$260 million
Unaudited pro forma adjusted consolidated net tangible asset value per Share ⁽³⁾	HK\$0.73	HK\$0.78

- (1) All statistics in this table are presented based on the assumption that options granted under the Pre-IPO Share Option Scheme are not exercised.
- (2) The calculation of market capitalisation is based on 200,000,000 Shares expected to be in issue immediately following the completion of the Capitalisation Issue and the Placing.
- (3) The unaudited pro forma adjusted consolidated net tangible asset value per Share is arrived at after the adjustments referred to in the section headed “Unaudited pro forma adjusted net tangible assets” in Appendix II to this prospectus and on the basis of 200,000,000 Shares expected to be in issue at the respective Placing Prices of HK\$1.10 and HK\$1.30 per Share immediately following the completion of the Capitalisation Issue and the Placing.

PRE-IPO SHARE OPTION SCHEME

Our Company has conditionally approved and adopted the Pre-IPO Share Option Scheme on 20 October 2011, the principal terms of which are summarised in the paragraph headed “Pre-IPO Share Option Scheme” in Appendix V to this prospectus. The purpose of the Pre-IPO Share Option Scheme is to give our Directors, senior management, consultants and other employees an opportunity to have a personal stake in our Company in order to motivate them to optimise their performance and efficiency, to reward them for their past contributions, and also to retain or otherwise maintain on-going relationships with them whose contributions are important to the long-term growth and profitability of our Group.

As of the Latest Practicable Date, options to subscribe for an aggregate of 1,300,000 Shares at an exercise price of 80% of the Placing Price have been granted by our Company under the Pre-IPO Share Option Scheme. Save for the options which have been granted as of the Latest Practicable Date, no further options will be granted under the Pre-IPO Share Option Scheme on or after the Listing Date.

Assuming all options granted under the Pre-IPO Share Option Scheme had been exercised in full on 1 January 2010 and 200,000,000 Shares to be in issue immediately following completion of the Capitalisation Issue and the Placing had been in issue throughout the year ended 31 December 2010, there would be a dilution effect of approximately 0.7% on the earnings per Share for the year ended 31 December 2010 from approximately 9.97 cents to approximately 9.90 cents.

SUMMARY

The options granted under the Pre-IPO Share Option Scheme represent 0.65% of the enlarged issued share capital of our Company immediately following completion of the Capitalisation Issue and the Placing. If all the options are exercised, there would be a dilution effect on the shareholding of our Shareholders of 0.65%.

SHARE OPTION SCHEME

Our Company has conditionally adopted the Share Option Scheme on 20 October 2011. The purpose of the Share Option Scheme is to provide the parties working for the interests of our Group with an opportunity to obtain an equity interest in our Company, thus linking their interest with the interests of our Group and thereby providing them with an incentive to work for the interests of our Group. As at the Latest Practicable Date, no share option has been granted pursuant to the Share Option Scheme. The principal terms of the Share Option Scheme are set out in the paragraph headed “Share Option Scheme” in Appendix V of this prospectus.

DIVIDEND POLICY

During the Track Record Period, and up to the Latest Practicable Date, save for the intra-group dividend of RMB9,932,359.61 declared to Renheng Tech from Baoying Renheng, we did not declare any dividends. As at the Latest Practicable Date, our Directors had no intention to distribute any other profits from Baoying Renheng. Our Company does not have any pre-determined dividend distribution ratio. The payment and the amount of any dividends, if paid, will depend on the results of operations, cash flows, financial condition, statutory and regulatory restrictions on the payment of dividends by our Group, future prospects and other factors that our Directors may consider relevant. The declaration, payment and amount of dividends will be subject to our Group’s discretion. Dividends may be paid only out of the distributable profits as permitted under the relevant laws. To the extent profits are distributed as dividends, such portion of profits will not be available to be reinvested in our Group’s operations. There can be no assurance that our Group will be able to declare or distribute any dividend in the amount set out in any plan of our Board or at all. The dividend distribution record in the past may not be used as a reference or basis to determine the level of dividends that may be declared or paid by our Group in the future.

RISK FACTORS

Risks relating to our Group

- Revenue derived from a limited number of products
- Unpredictable nature of revenue and profitability
- Reliance on major customers
- Reliance on single production plant
- Failure of renewal of the Tobacco Production Licence

SUMMARY

- Decrease in the level of capital spending by cigarette manufacturers and tobacco redrying factories in the PRC
- Reliance on key management personnel
- Failure to offer technologically improved products
- Constraints of our manufacturing capacity
- Delays in payments by customers
- Postponement in delivery/installation schedule requested by our customers/end customers
- Handling fee payable to CTMC
- Fluctuations in the prices of raw materials, parts and components or shortage of raw material, part and component supplies
- Pricing of catalogued special-purpose tobacco machinery
- Increase in labour costs
- Effects of fluctuations in our gross profit margins and change in product mix on our operating results
- Net operating cash outflow and overall net cash outflow incurred for the six months ended 30 June 2011
- Possible infringement of our intellectual property rights
- Potential product liability claims
- Exposure to environmental liabilities
- Occupational hazards
- Limited insurance coverage for our production facilities
- Historical advancing activities
- Future dividend policy
- Failure to implement our future plans

SUMMARY

- Uncertainties with respect to the development of our hot stamped foil trading business
- Our tobacco machinery products have long average replacement cycle

Risks relating to the industry

- Competition from other tobacco machinery manufacturers
- Enforcement of tobacco control regulations in the PRC
- Effect of change in demand of tobacco products resulting from health hazard awareness and social advocacy for tobacco control
- Effect of changes in the PRC laws, rules and regulations regarding catalogued special-purpose tobacco machinery industry

Risks relating to the PRC

- Effect of changes in the PRC economic, political and social conditions and government policies
- Uncertainties with respect to the PRC legal system
- If the favourable tax treatments that we currently receive are altered or eliminated, our results of operations may be adversely affected
- PRC regulations on loans to and direct investment by offshore holding companies in PRC entities may delay or prevent us from using the proceeds from the Placing to make loans or additional capital contributions to our PRC subsidiary
- Fluctuations in the value of RMB and government control over currency exchange could adversely affect our business, operating results and financial condition
- Enforcement of the labour contract law and other labour-related regulations in the PRC
- Significant uncertainties under the new enterprise income tax law relating to our PRC enterprise income tax liabilities
- Uncertainties regarding the regulatory requirements on statutory reserves
- Natural disasters, acts of war, political unrest and epidemics
- Tightening of credit in the PRC

SUMMARY

Risks relating to the Placing

- Termination of the Underwriting Agreement
- No prior public market for the Shares
- Trading price and trading volume of the Shares may be volatile
- Dilution of Shareholders' equity interests as a result of additional equity fund raising or the exercise of the share options granted by our Company
- The laws of the Cayman Islands relating to the protection of interest of minority shareholders may be different from those in Hong Kong

Risks relating to the prospectus

- Potential unreliability of facts and statistics with respect to information obtained from various official government sources
- Potential unreliability of facts and statistics with respect to information contained in the press articles or other media regarding our Company and the Placing
- Forward-looking statements

DEFINITIONS

In this prospectus, unless the context otherwise requires, the following expressions shall have the following meanings:

“Articles of Association” or “Articles”	the articles of association of the Company adopted on 20 October 2011 and as amended from time to time
“associate(s)”	has the meaning ascribed thereto under the GEM Listing Rules
“Atlas”	the third edition of the Tobacco Atlas published by the American Cancer Society and World Lung Foundation in 2009
“Baoying Hengda”	寶應縣恒達煙機廠 (Baoying Hengda Tobacco Machinery Factory*), a domestic company incorporated in China on 24 October 2001 by 69 former employees of 寶應縣無線電廠 (Baoying Radio Factory*) and a former shareholder of Baoying Renheng
“Baoying Renheng”	寶應仁恒實業有限公司 (Bao Ying Ren Heng Industrial Co., Ltd*), a wholly foreign owned company incorporated in China on 1 November 2001, and an indirect wholly-owned subsidiary of the Company
“Board”	the board of Directors
“business day(s)”	any day(s) (excluding Saturdays, Sundays and public holidays) in Hong Kong on which licensed banks in Hong Kong are generally open for normal banking business to the public
“BVI”	the British Virgin Islands
“CAGR”	compound annual growth rate
“Capitalisation Issue”	the issue of Shares to be made upon capitalisation of certain sums standing to the credit of the share premium account of the Company as referred to in the paragraph headed “Written resolutions of the Shareholders” in Appendix V to this prospectus
“CCASS”	the Central Clearing and Settlement System established and operated by HKSCC
“CCASS Clearing Participant”	a person admitted to participate in CCASS as a direct clearing participant or general clearing participant

DEFINITIONS

“CCASS Custodian Participant”	a person admitted to participate in CCASS as a custodian participant
“CCASS Investor Participant”	a person admitted to participate in CCASS as an investor participant who may be an individual or joint individuals or a corporation
“CCASS Participant”	a CCASS Clearing Participant or a CCASS Custodian Participant or a CCASS Investor Participant
“China Tobacco Year Book”	中國煙草年鑑 (the China Tobacco Yearbook) issued by STMA
“CNTC”	中國煙草總公司 (China National Tobacco Corporation), a State-owned company incorporated in the PRC on 15 December 1983, and an Independent Third Party
“Companies Law”	the Companies Law (2010 Revision) of the Cayman Islands, as amended, supplemented or otherwise modified from time to time
“Companies Ordinance”	Companies Ordinance (Chapter 32 of the Laws of Hong Kong), as amended, supplemented or otherwise modified from time to time
“Company” or “our Company”	RENHENG Enterprise Holdings Limited (仁恒實業控股有限公司), a company incorporated in the Cayman Islands with limited liability on 2 February 2011 under the Companies Law
“connected person(s)”	has the meaning ascribed thereto under the GEM Listing Rules
“Controlling Shareholder(s)”	Mr. Wei, Ms. Liu, LinkBest and Open Venture who are entitled to control, in aggregate, the exercise of 75% of the voting rights at general meetings of the Company immediately after completion of the Capitalisation Issue and the Placing
“CTMC”	中國煙草機械集團有限責任公司 (China Tobacco Machinery (Group) Co., Ltd.*), a company incorporated in the PRC on 7 January 1988 which is owned as to 67% by CNTC, and an Independent Third Party
“Director(s)”	the director(s) of the Company

DEFINITIONS

“EIT Law”	中華人民共和國企業所得稅法 (The PRC Enterprise Income Tax Law), which is promulgated by the National People’s Congress and took effect on 1 January 2008
“FIE”	foreign-invested enterprises incorporated under the laws of the PRC
“Foreign Investors M&A Rules”	關於外國投資者併購境內企業的規定 (Rules on the Acquisition of Domestic Enterprises by Foreign Investors*)
“GEM”	the Growth Enterprise Market of the Stock Exchange
“GEM Listing Rules”	the Rules Governing the Listing of Securities on GEM, as amended from time to time
“Grand Bright”	Grand Bright International Enterprise Limited (明泰國際企業有限公司), a limited company incorporated in Hong Kong on 27 September 1999, which is held as to 95% by Mr. Wei and 5% by Ms. Liu
“Group” or “our Group” or “we” or “us”	the Company and its subsidiaries or, where the context so requires, in respect of the period before the Company became the holding company of its present subsidiaries, the present subsidiaries of the Company or their predecessors (as the case may be)
“GTSS”	Global Tobacco Surveillance System, developed by the World Health Organization, the Centers for Disease Control and Prevention, and the Canadian Public Health Association in 1999
“HK Hongta”	Hong Kong Hongta International Tobacco Company Limited (香港紅塔國際煙草有限公司), a company incorporated in Hong Kong on 25 June 1992, which is held as to 55% by Hongta Tobacco (Group) Ltd., Co., 30% by Yanlord International Investment Company Limited and 15% by Yunnan Tobacco International Company Limited, and an Independent Third Party
“HKFRS”	Hong Kong Financial Reporting Standards
“HKSCC”	Hong Kong Securities Clearing Company Limited
“Hong Kong” or “HK”	the Hong Kong Special Administrative Region of the PRC

DEFINITIONS

“Hongta Renheng”	珠海經濟特區紅塔仁恒紙業有限公司 (Zhuhai S.E.Z. Hongta Renheng Paper Co., Ltd.*), a company incorporated in the PRC on 11 February 1991 and a subsidiary of Foshan Huaxin Packaging Co., Ltd. (佛山華新包裝股份有限公司), which is listed on Shenzhen Stock Exchange (Stock code: 200986), and an Independent Third Party
“Independent Third Party(ies)”	person(s) or company(ies) which is/are independent of and not connected with any of the Directors, chief executive or substantial shareholders of the Company or any of its subsidiaries or any of their respective associates
“Jinchuang”	揚州金窗幕牆工程有限公司 (Yangzhou Jinchuang Curtain Wall Engineering Company Limited*), a company incorporated on 9 June 2005 in the PRC and a wholly owned subsidiary of Yanlord Industry Investment
“JSTD”	江蘇省科學技術廳 (Jiangsu Science and Technology Department)
“Latest Practicable Date”	24 October 2011, being the latest practicable date prior to the printing of this prospectus for ascertaining certain information contained in this prospectus
“LinkBest”	LinkBest Capital Group Limited, a company incorporated in BVI on 1 July 2010 with limited liability which is wholly owned by Mr. Wei
“Listing”	the listing of the Shares on GEM
“Listing Date”	the date on which the trading of the Shares first commences on GEM
“Longtai”	揚州龍泰電氣有限公司 (Yangzhou Longtai Electric Company Limited*), a company incorporated in the PRC on 29 April 2007, and a wholly owned subsidiary of Yanlord Industry Investment
“Main Board”	the stock market operated by the Stock Exchange prior to the establishment of GEM (excluding the options market) and which stock market continues to be operated by the Stock Exchange in parallel with GEM and which, for the avoidance of doubt, excludes GEM

DEFINITIONS

“Measures on Administration of Procurement”	煙草專用機械購置管理辦法(Measures on Administration of Procurement of Catalogued Special-purpose Tobacco Machinery) promulgated by STMA and took effect on 24 July 2006
“Mr. Wei”	Mr. Wei Sheng Peng (魏勝鵬), one of the founders and an executive Director
“Ms. Liu”	Ms. Liu Li (劉利), an executive Director and the spouse of Mr. Wei
“New Land”	a piece of land with a site area of approximately 62,741 sq.m. situated at No.18, North Suzhong Road, Baoying County, Yangzhou, Jiangsu Province, the PRC
“Non-Competition Undertaking”	a deed of non-competition undertaking dated 20 October 2011 executed by LinkBest, Open Venture, Mr. Wei and Ms. Liu in favour of the Company as referred to under the paragraph headed “Non-competition undertaking” in the section headed “Controlling Shareholders and substantial Shareholders” in this prospectus
“Notice 75”	關於境內居民通過境外特殊目的公司融資及返程投資外匯管理有關問題的通知 (Notice on Issues Relating to the Administration of Foreign Exchange in Fund-raising and Reverse Investment Activities of Domestic Residents Conducted via Offshore Special Purpose Vehicles) promulgated by the PRC State Administration of Foreign Exchange on 21 October 2005 and effective on 1 November 2005
“Old Land”	a piece of land with a site area of approximately 10,383 sq.m. situated at No.1 East Yeting Road, Baoying County, Yangzhou, Jiangsu Province, the PRC
“Open Venture”	Open Venture Global Limited, a company incorporated in BVI on 8 October 2010 with limited liability which is wholly owned by Ms. Liu
“PBOC”	the People’s Bank of China (中國人民銀行), the central bank of the PRC
“Placing”	the conditional placing by the Underwriter on behalf of the Company of the Placing Shares for cash at the Placing Price on and subject to the terms and conditions stated in this prospectus

DEFINITIONS

“Placing Price”	the price for each Placing Share of not more than HK\$1.30 per Placing Share (exclusive of any brokerage, Stock Exchange trading fee and SFC transaction levy)
“Placing Shares”	the aggregate of 50,000,000 Shares being offered at the Placing Price under the Placing
“PRC” or “China”	The People’s Republic of China which shall, for the purpose of this prospectus, exclude Hong Kong, the Macau Special Administration Region of the PRC and Taiwan
“PRC Government” or “State”	the central government of the PRC, including all governmental subdivisions (including provincial, municipal and other regional or local government entities) and instrumentalities thereof, or, where the context requires, any of them
“PRC Legal Advisers”	Grandall Legal Group (Shenzhen), engaged as our Company’s legal advisers as to PRC law
“Pre-IPO Share Option Scheme”	the pre-IPO share option scheme conditionally adopted by the Company on 20 October 2011, the principal terms of which are set out in the paragraph headed “Pre-IPO Share Option Scheme” in Appendix V to this prospectus
“Price Determination Date”	the date expected to be on or around 9 November 2011, or such later date as agreed by the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter), on which the Placing Price is fixed by agreement between the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) for the purpose of the Placing
“Pricing Approval 2010”	國家煙草專賣局關於SJ41型糖香料廚房系統等煙機產品出廠價格的批覆(the Approval of STMA Regarding the Ex-factory Prices of Tobacco Machinery Products including Casing and Flavouring System Model SJ41) issued by STMA on 22 April 2010 and became effective on 23 April 2010, being the approval in response to applications for guidance price of casing and flavouring systems produced by several tobacco machinery manufacturers, including our Group
“Pricing Guidelines”	2004年全國煙草專用機械產品指導價格目錄(暫行) (the 2004 Provisional Pricing Guidelines on the Pricing of Catalogued Special-purpose Tobacco Machinery*) issued by STMA

DEFINITIONS

“Renheng Global”	RENHENG Global Limited (仁恆環球有限公司), formerly known as Yanlord Global Limited, a company incorporated in BVI on 15 October 2009 with limited liability and a wholly-owned subsidiary of the Company
“Renheng Tech”	RENHENG Tech Limited (仁恆科技有限公司), formerly known as Yanlord Tech Limited, an investment holding company incorporated in Hong Kong on 28 October 2009 and an indirect wholly-owned subsidiary of the Company
“Reorganisation”	the corporate reorganisation of the Group effected in preparation for the Listing as described under the subparagraph headed “Corporate Reorganisation” in the paragraph headed “Further information about the Company and its subsidiaries” in Appendix V to this prospectus
“SAFE”	中國國家外匯管理局 (the PRC State Administration of Foreign Exchange)
“SFC”	Securities and Futures Commission of Hong Kong
“SFO”	Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) as amended or otherwise modified from time to time
“Share(s)”	share(s) of HK\$0.01 each in the share capital of the Company
“Share Option Scheme”	the share option scheme conditionally adopted by the Company on 20 October 2011, the principal terms of which are set out in the paragraph headed “Share Option Scheme” in Appendix V to this prospectus
“Shareholder(s)”	holder(s) of the Share(s)
“Shenyin Wanguo” or “Sponsor” or “Lead Manager”	Shenyin Wanguo Capital (H.K.) Limited, a corporation licensed to carry on type 1 (dealing in securities), type 4 (advising on securities) and type 6 (advising on corporate finance) regulated activities under the SFO, being the sponsor to the Listing and the lead manager of the Placing
“State Council”	中華人民共和國國務院 (State Council of the PRC)
“STMA”	中國國家煙草專賣局 (State Tobacco Monopoly Administration of the PRC), a division of the PRC government established on 1 November 1983

DEFINITIONS

“Stock Exchange”	The Stock Exchange of Hong Kong Limited
“subsidiary(ies)”	has the meaning ascribed thereto in section 2 of the Companies Ordinance
“substantial shareholder(s)”	has the meaning ascribed thereto under the GEM Listing Rules
“Tobacco Machinery Documents”	collectively refer to the Tobacco Machinery List, the Pricing Guidelines and the Pricing Approval 2010
“Tobacco Machinery List”	煙草專用機械名錄 (List of Catalogued Special-purpose Tobacco Machinery*) issued by STMA on 24 May 2004 and became effective on 1 June 2004
“Tobacco Production Licence”	煙草專賣生產企業許可證 (tobacco monopoly production enterprise licence*) issued by STMA
“Track Record Period”	the period comprising the two financial years ended 31 December 2010 and the six months ended 30 June 2011
“Underwriter”	the underwriter in respect of the Placing named in the section headed “Underwriting” in this prospectus
“Underwriting Agreement”	the underwriting agreement entered into on 27 October 2011 between the Company, the executive Directors, the Controlling Shareholders and Shenyin Wanguo (in the respective capacity as the Sponsor, the Lead Manager and the Underwriter), particulars of which are summarised in the section headed “Underwriting” in this prospectus
“WFOE”	wholly foreign owned enterprise incorporated and registered under the laws of the PRC
“Yanlord Industrial”	Yanlord (Holdings) Industrial Limited (仁恆集團實業有限公司), a company incorporated in Hong Kong on 21 July 1992 which is owned as to 95% by Mr. Zhong Sheng Jian and 5% by Mr. Wei
“Yanlord Industry Investment”	Yanlord Industry Investment Limited (仁恆工業投資有限公司), a company incorporated in Hong Kong on 14 May 2005 which is owned as to 60% by Mr. Wei and 40% by Ms. Liu

DEFINITIONS

“Zhuhai Mingtai”	珠海明泰精細化工有限公司 (Zhuhai Mingtai Fine Chemical Company Limited*), a company incorporated in China on 20 January 2000, which is indirectly beneficially held as to 95% by Mr. Wei and 5% by Ms. Liu
“HK\$” or “Hong Kong dollars” and “cents”	Hong Kong dollars and cents, respectively, the lawful currency of Hong Kong
“RMB” or “Renminbi”	Renminbi, the lawful currency of the PRC
“sq.m. or m ² ”	square metre(s)
“%”	per cent.

* *denotes English translation of the Chinese name and is provided for identification purpose only*

For ease of reference, the English version of the Chinese names of companies, entities, departments, associations, legislation and addresses in the PRC which are included in this prospectus are for identification purposes only, and should not be regarded as the official English translation of such Chinese names or words unless stated otherwise. In the event of inconsistency, the Chinese version shall prevail.

GLOSSARY

This glossary contains explanations of certain terms used in this prospectus. These terms and their meanings may not correspond to standard industry meanings or usage of these terms.

“casing and flavouring system”	an automated system designed for the purpose of creating the signature taste of cigarettes by blending numerous kinds of flavours and casings according to the unique recipes of individual cigarette brands (煙用香精香料調配及加料加香機械)
“catalogued special-purpose tobacco machinery”	any type of tobacco machinery listed on the Tobacco Machinery Documents
“CNC press brake”	computerised numerical control press brake which is a piece of equipment for bending metal sheets and metal plates (數控折彎機)
“dedusting system ”	a system that is equipped with tobacco machinery to perform dust removal functions (煙用除塵系統)
“feeding system”	a mechanical system used to deliver various types of material such as cut tobacco, filter and cigarette packages during the cigarette production process (煙用輸送機械)
“filter rod forming machine”	a machine used to manufacture filter rods for cigarettes (嘴棒成型機)
“ISO”	International Organization for Standardization, a non-governmental organisation based in Geneva, Switzerland that develops and publishes international standards
“ISO 9001:2008”	a set of requirements developed by ISO for a quality management system where an organisation (i) needs to demonstrate its ability to consistently provide product that meets customer and applicable statutory and regulatory requirements; and (ii) aims to enhance customer satisfaction through the effective application of the system, including processes for continual improvement of the system and the assurance of conformity to customer and applicable statutory and regulatory requirements
“PF system”	pneumatic feeding system, which is a type of pneumatic-based feeding system used to deliver the processed cut tobacco inside an enclosed piping system to the cigarette wrapping machine (風力送絲系統)

GLOSSARY

“PP system”	pre-pressing packing machine, a piece of equipment to compress and pack tobacco leaves (煙用預壓打包機械)
“swelling agent delivery system”	an automated device that delivers the swelling agent to the filter rod forming machine (嘴棒成型機膨化劑集中輸送系統)

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Potential investors of the Placing Shares should carefully consider all of the information contained in this prospectus and, in particular, the following risk factors and special considerations associated with an investment in our Company before making any investment decision in relation to our Company. The information in respect of the market position or the market share of our Group is not presented in this prospectus as no official statistics of the tobacco machinery market is available from the relevant government authorities, industry bodies, research agencies and/or other reliable public domain. Our Group's business, financial condition or results of operations could be materially and adversely affected by any of these risks or other risk factors and uncertainties that our Company is unaware of, or investment factors that our Company considers insignificant at present. The trading price of the Shares may decline due to any of these risk factors and uncertainties, and you may lose all or part of your investment in the Shares.

RISKS RELATING TO OUR GROUP

Revenue derived from a limited number of products

Our revenue was generated principally from the sale of three types of catalogued special-purpose tobacco machinery products, namely casing and flavouring system, PF system and PP system, and related components and/or devices not listed in all of the Tobacco Machinery Documents, which in aggregate accounted for approximately 92.6%, 95.4% and 93.0% of our turnover for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. If demand for such products drops as a result of competition, technological changes, or slowdown of growth in the PRC tobacco industry, our results of operations will be materially and adversely affected.

Unpredictable nature of revenue and profitability

We conduct our tobacco machinery product business on a project basis and all of our products are custom-made to meet the needs of cigarette manufacturers and tobacco redrying factories in the PRC. The types and units of products supplied may vary significantly from time to time depending on the projects undertaken by us. The value of our tobacco machinery projects also varies depending on the scope, types and complexity of the products and services provided. As our revenue and income is derived from sales contracts on a project-by-project basis, the revenue of our Group tends to be non-recurring in nature and the profitability of our Group is therefore unpredictable. There is no assurance that we can secure projects which will generate revenue at levels as those previously received by our Group.

Reliance on major customers

The end customers of our products and services are generally cigarette manufacturers and tobacco redrying factories in the PRC. Pursuant to the Measures on Administration of Procurement promulgated by STMA in 2004, CTMC monitors and oversees all domestic tobacco machinery procurement matters between the tobacco machinery manufacturers and the cigarette manufacturers, and we enter into contracts directly with CTMC instead of the cigarette manufacturers and tobacco redrying factories in providing our catalogued special-purpose tobacco machinery products as listed in

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all of the Tobacco Machinery Documents to the end customers. By virtue of our contractual relationship with CTMC under the aforesaid regulatory requirements in respect of catalogued special-purpose tobacco machinery procurement arrangements, CTMC was our largest customer during the two years ended 31 December 2010 and was our second largest customer during the six months ended 30 June 2011 and accounted for approximately 73.3%, 66.1% and 33.9% of our turnover for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. Nevertheless, the end customers of our catalogued special-purpose tobacco machinery are generally cigarette manufacturers (in the case of our casing and flavouring systems and PF systems) and tobacco redrying factories (in the case of our PP systems). During the Track Record Period, our top five end customers together accounted for approximately 65.2%, 72.3% and 93.6% of our turnover respectively. For the year ended 31 December 2009, the single largest end customer accounted for approximately 21.0% of our turnover for the year whilst for the year ended 31 December 2010, the single largest end customer, not related to the single largest end customer in 2009, accounted for approximately 24.8% of our turnover for the year. For the six months ended 30 June 2011, our single largest end customer, not related to the single largest end customer in 2009 and 2010, accounted for approximately 79.7% of our turnover for the period. Accordingly, our revenue and profitability in a year would depend on a small number of end customers. If we are unable to grow our end customer base or any of our major end customers terminates to purchase from us, our revenue and profitability would be adversely affected.

Reliance on single production plant

All of our existing production facilities are located at one location in Baoying County, Jiangsu Province, the PRC. Any damages to or destruction of our production facilities arising from unexpected or catastrophic events, which results in interruption in, or prolonged suspension of, our production at that location would have a material and adverse impact on our operation, financial condition and results of operation.

Failure of renewal of the Tobacco Production Licence

We possess the Tobacco Production Licence under which we are permitted to manufacture and sell our three major products, namely casing and flavouring system, PF system and PP system. Pursuant to the 煙草專賣許可證管理辦法 (Measures on Administration of Tobacco Monopoly Licence), the maximum duration of validity of the Tobacco Production Licence is five years, subject to renewal by the STMA after its expiry. Our current Tobacco Production Licence is valid for a period of five years commencing on 14 April 2009 and expiring on 14 April 2014. However, there is no assurance that we will be able to renew the Tobacco Production Licence from time to time. Any failure to renew our Tobacco Production Licence in the future may adversely affect our business, results of operations and financial condition.

Decrease in the level of capital spending by cigarette manufacturers and tobacco redrying factories in the PRC

During the Track Record Period, all of our revenue was derived from sales in the PRC. The demand for our tobacco machinery products depends significantly on the level of installing, replacement and maintenance activities of cigarette manufacturers and tobacco redrying factories in the PRC, which

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in turn depends on the level of capital spending by such cigarette manufacturers and tobacco redrying factories. As discussed in the sub-paragraph headed “Consolidation of PRC tobacco industry” under the paragraph headed “Tobacco industry in the PRC” in the section headed “Industry overview” in this prospectus, the fixed asset investment in the tobacco products industry in urban areas grew at a CAGR of approximately 20.1% between 2004 and 2009 while the fixed asset investment in relation to equipment purchasing in the tobacco products industry in urban areas increased at a CAGR of approximately 13.5% in the same period. However, there is no assurance that the fixed asset investment in relation to equipment purchasing in the tobacco products industry in China will continue to grow at the same rate as discussed above or that its growth will be steady in the coming future. In addition, any decrease in the level of capital spending by cigarette manufacturers and tobacco redrying factories in the PRC could have an adverse effect on our business, financial position and results of operations.

Reliance on key management personnel

Our success depends, to a significant extent, on the expertise and experience of the key members of our management team. Mr. Wei, chairman of our Board, has more than 14 years of experience in the electrical and mechanical equipment industry. Mr. Sun Zhaohui, one of our executive Directors, the chief executive officer of our Company and the legal representative of Baoying Renheng, has no less than 10 years of engineering experience. Mr. Xu Jiagui, a director and general manager of Baoying Renheng, has over 8 years of research and development, production and general management experience relating to the tobacco machinery manufacturing industry. Mr. An Zhanqi, the chief engineer of Baoying Renheng, has no less than 9 years of experience in the engineering field. Their continuous service is critical to our operation and financial performance. If we were unable to retain our key management personnel or recruit competent personnel to replace any possible loss of such key management personnel in a timely manner, or were unable to engage other qualified personnel to join our management for our development, our future operations may be adversely affected.

Failure to offer technologically improved products

We believe that the users of our products, being mainly cigarette manufacturers in the PRC, are focused on continuous technological improvements in their cigarette production process. As a result, we must continuously develop new and innovative products in order to maintain our competitiveness. There is no assurance that we will be able to develop technologically improved products, or successfully launch such products in a timely manner. Furthermore, our competitors may be able to offer more technologically advanced products that may better meet the evolving requirements of the cigarette manufacturers and tobacco redrying factories. Any occurrence of these events may have a material adverse effect on the demand for our products.

Our Directors intend to apply approximately 71.2% of the net proceeds from the Placing on continuous product development and innovation. However, the research and development projects may not be successful, and the related costs which would be expensed will have an adverse impact on our financial position.

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Constraints of our manufacturing capacity

Our manufacturing capabilities are limited by our production capacity. We estimate that our utilisation rate was approximately 93.9%, 111.0% and 134.2% respectively during the Track Record Period. Please refer to the sub-paragraph headed “Production facilities and production capacity” in the paragraph headed “Production” in the section headed “Business” in this prospectus for further details in respect of our production capacity and utilisation rates. We may increase our production capacity by either upgrading our existing facilities and equipment, purchasing new equipment, recruiting additional workers or outsourcing our work to third parties. There is no guarantee that we will be able to acquire the equipment in a timely manner or at a reasonable price, hire an adequate number of suitable employees, or appoint additional qualified subcontractors to undertake our production work. Any failure to expand our production capacity in a timely manner may adversely affect our operations and growth prospects.

Delays in payments by customers

With regard to the sales of our casing and flavouring systems, PF systems and PP systems, we normally receive an initial payment of 20% of the contract value after signing the sales contracts. Therefore, we may have to pay in advance certain costs and expenses in relation to some of the contracts prior to receiving adequate funds to cover such costs and expenses. Average trade receivable turnover days were approximately 44 days, 41 days and 39 days in 2009, 2010 and in the first half of 2011 respectively which remained within the credit period of three months normally granted to our customers. As at 30 June 2011, our net trade receivables aged over 90 days were at approximately HK\$7,158,000 of which approximately HK\$2,286,000 were subsequently settled up to 31 August 2011. Of the outstanding balance of approximately HK\$4,872,000, an aggregate amount of approximately HK\$4,301,000 was due from eight customers in relation to existing projects. The slow settlement was mainly due to additional modifications requested by the customers and delay in the customers’ internal payment process to settle their balances due to us. Among these eight customers, five of them have contracted with our Group for other projects which have not yet been completed as at 31 August 2011, and we expect that these projects will be completed by December 2012. Meanwhile, provisions for doubtful debt of approximately HK\$288,000 were made on the long outstanding trade balances during the six months ended 30 June 2011 after considering the nature of the trade receivables and their collectability. Any delay in payment(s) by our customers, where the relevant amount(s) of payment(s) is or are financially significant, individually or collectively, may materially and adversely affect our working capital position.

Postponement in delivery/installation schedule requested by our customers/end customers

During the Track Record Period, 26, 29 and 8 contracts for which revenue had been recognised, representing approximately 67.2%, 80.4% and 92.8% of our turnover respectively, have experienced postponement in delivery/installation schedule requested by our customers/end customers for periods ranging from approximately 1 month to 10 months. In respect of contracts signed but not completed as at 31 August 2011, we have experienced postponement in delivery/ installation schedule requested by customers for periods up to 22 months. For further information of these contracts, please refer to the sub-paragraph headed “Contracts signed but not completed as at 31 August 2011” under the paragraph headed “Products and services” in the “Business” section in this prospectus.

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Generally, for our sales of casing and flavouring systems, PF systems and PP systems, we receive an initial payment of 20% of the contract value after signing the sales contracts and 70% of the contract value upon delivery of our products. As regards our non-catalogued ancillary tobacco machinery products and the provision of maintenance, overhaul and modification services, we generally receive an initial payment ranging from 10% to 30% of the contract value upon signing the contracts, and another payment of up to 90% of the contract value upon completion of the product installation and testing or completion of the services. For sales and services contracts without initial payment, we generally receive a payment of up to 90% of the contract value upon completion of the product installation and testing or completion of the services. Therefore, we may have to pay in advance certain costs and expenses prior to the delivery/installation of the products. In cases where the delivery date is not specified or is subject to customer's instruction pursuant to the terms in the sale and purchase agreement, we are not entitled to any compensation from the customers for the postponement in delivery/installation schedule requested by them. In other cases where the delivery date is specified in the sale and purchase agreement, despite the fact that we are entitled to compensation from the customer for postponement under relevant PRC laws, we in general will still accommodate the customer's request to defer product delivery/installation to meet their operation needs. Our Directors are of the view that our revenue attributable to these contracts was not material during the Track Record Period.

Any delay in postponement in delivery/installation schedule of a project, where the amount of payment upon delivery/completion of installation is financially significant, may materially and adversely affect our working capital position.

Handling fee payable to CTMC

During the Track Record Period, we paid handling fees to CTMC at 3% of the value of the contracts entered into between our Group and CTMC in respect of our sales of catalogued special-purpose machinery products. The amounts were not paid separately by us, but were deducted by CTMC directly from its progress payments made to our Group. As at 31 December 2009 and 2010 and 30 June 2011, we had no handling fee payable to CTMC as the trade receivables due from CTMC had been fully settled. In view of the current settlement arrangements amongst CTMC, our Group and the end customers in respect of the procurements of catalogued special-purpose machinery products as set out in the paragraph headed "Business model" in the section headed "Business" in this prospectus, our Directors believe that we are still liable to the handling fee payable to CTMC if an end customer defaults on its payment to CTMC for the purchase of our products. Any demand from CTMC for the settlement of the handling fees prior to receiving payment from CTMC in relation to the relevant contracts may have an adverse effect on our business, financial condition and results of operations.

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Fluctuations in the prices of raw materials, parts and components or shortage of raw material, part and component supplies

While we price our catalogued special-purpose tobacco machinery products in accordance with (i) the 5% range of the guidance price in the Pricing Guidelines and (ii) the Pricing Approval 2010, we determine the contract price based on our estimated project costs at the time we submit a proposal to our potential customers or our tenders for projects. After we have entered into a sales contract with our customers, we may then procure the necessary raw materials, parts and components. There is a time lapse between the submission of proposals or tenders and the procurement of raw materials, parts and components. As such, any fluctuation in the prices of raw materials, parts and components as well as other costs in our initial project cost estimation during the interim period may adversely affect our business, financial condition and results of operations.

We currently procure raw materials, parts and components from various suppliers. However, there is no assurance that we will be able to secure adequate supply of such raw materials, parts and components to meet our production requirements. Any shortage in raw material, part and component supplies may have an adverse effect on our business, financial condition and results of operations.

Pricing of catalogued special-purpose tobacco machinery

The pricing of our catalogued special-purpose tobacco machinery is subject to the Pricing Guidelines and the Pricing Approval 2010. In the event that the guidance price of a catalogued special-purpose tobacco machinery product specified in the Pricing Guidelines or the Pricing Approval 2010 is not able to cover the costs of production at times of increasing costs, and our application to STMA requesting for a revision of the guidance price is not successful, our business, financial condition and results of operations may be adversely affected.

Increase in labour costs

Substantially all of our operations are conducted in the PRC. During the Track Record Period, direct labour costs accounted for approximately 2.6%, 2.6% and 1.6% of our costs of sales respectively. There is no assurance that labour costs in the PRC will not increase in the future. If our labour costs increase and we cannot pass such increase on to our customers, our business, financial condition and results of operations may be adversely affected.

Effects of fluctuations in our gross profit margins and change in product mix on our operating results

During the Track Record Period, we generated the majority of our turnover from the manufacture, sale and provision of maintenance, overhaul and modification services in respect of three types of catalogued special-purpose tobacco machinery products, namely casing and flavouring systems, PF systems and PP systems, and related components and devices not listed in all of the Tobacco Machinery Documents whilst a minority of our turnover was derived from the manufacture, sale and provision of maintenance, overhaul and modification services in respect of non-catalogued ancillary tobacco

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machinery products. Our different product categories have historically experienced different gross margins which fluctuated during the Track Record Period. The following table sets forth our gross profit margin by project category during the Track Record Period:

	For the year ended 31 December		Six months ended 30 June
	2009	2010	2011
	%	%	%
Catalogued special-purpose tobacco machinery projects			
Casing and flavouring systems	33.9	36.6	30.2
PF systems	63.2	65.7	57.8
PP systems	30.7	56.3	43.4
Sub-total	39.0	44.5	31.4
Non-catalogued ancillary tobacco machinery projects and other products			
	40.9	40.7	43.8
Total	39.1	44.3	32.3

We conduct our tobacco machinery product business on a project basis and all of our products are custom-made to meet the needs of cigarette manufacturers and tobacco redrying factories in the PRC. The types and units of product supplied may vary significantly from time to time depending on the projects undertaken by us. As the gross margins of our products vary, any change in the product mix of our turnover will affect our results of operations from period to period.

Net operating cash outflow and overall net cash outflow incurred for the six months ended 30 June 2011

We incurred net operating cash outflow of approximately HK\$12,005,000 and total net cash outflow of approximately HK\$15,804,000 for the six months ended 30 June 2011, which were mainly attributable to the increase in inventories and amounts due from customers for contract work and decrease in amount due to a customer for contract work in relation to our projects in progress. We also incurred listing expenses of approximately HK\$2,225,000 and paid PRC enterprise income tax of approximately HK\$7,790,000 during the period. We cannot give any assurance that we will not have periods of net operating cash outflow or overall net cash outflow in the future. In the event that we are unable to generate sufficient cash flow for our operations or otherwise unable to obtain sufficient funds to finance our business, our operations may be materially and adversely affected. There can also be no assurance that we will maintain sufficient working capital, generate adequate revenues or raise necessary funding to pay off our current liabilities and meet our capital commitments in a timely manner. In such circumstances, our financial and liquidity positions, business operations and prospects may be materially and adversely affected.

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Possible infringement of our intellectual property rights

In order to protect our rights over our intellectual property, we have obtained certain patents in the PRC and have applied for the registration of certain patents regarding our tobacco machinery products in the PRC. Please refer to the paragraph headed “Further information about the business of the Group – Intellectual property rights of the Group” in Appendix V to this prospectus for more details. There is no assurance that these measures will be adequate to prevent infringement of our intellectual property rights by third parties, or that our patent registration applications would not be delayed or refused by the relevant PRC governmental authorities. If we are not able to adequately protect our intellectual property rights, our financial position, business and operating results may be adversely affected.

Potential product liability claims

We do not maintain any insurance in respect of the product liability risk in the PRC. In the event that any of our products is alleged to have caused any personal injury or other adverse effects, we may be subject to product liability claims under the PRC law. The PRC Legal Advisers have advised that product liability insurance is not compulsory for tobacco machinery manufacturers under the PRC law. Accordingly, we do not maintain insurance coverage for product liability. Any lawsuit or proceeding brought against us in respect of the product liability claim will be costly and time-consuming and adversely affect our financial performance. There is no assurance that we will not be subject to product liability claims or other claims in the future. Any successful claim made against us which is not covered by our existing insurance policies, or is in excess of our insurance coverage, may have a material adverse impact on our business, financial position and results of operations.

Exposure to environmental liabilities

Under the relevant environmental protection laws and regulations in the PRC, the construction, expansion and operation of production facilities are subject to certain government evaluation process, inspection procedures and approvals. Failure to go through such government process or procedures or to obtain such government approvals may subject us to fines and penalties imposed by the relevant PRC environmental authorities, including suspension of the production facilities. Moreover, as our production process generates waste water, exhausted gas, noise and other wastes, we are also required to comply with applicable national and local environmental regulations. Any failure by us to comply with the present or future applicable environmental regulations could subject us to substantial fines, suspensions in our production or cessation of our operations, which would have a material adverse impact on our business and results of operations.

In addition, there is no assurance that future changes in PRC environmental protection laws and regulations will not impose costly compliance requirements on our Group or otherwise subject us to future liabilities. Any such law or regulation applicable to the manufacture of our products may require us to incur significant capital expenditure or increase our operating costs.

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Occupational hazards

Our business operations involve occupational hazards that are inherent to the industry and which may not be completely eliminated through the implementation of preventive measures. These occupational risks may result in personal injury, damage to or destruction of our properties or our production facilities. As a result, our business, financial condition and results of operations may be adversely affected if we incur any loss which is not covered by our existing insurance policies or is in excess of our insurance coverage.

Limited insurance coverage for our production facilities

We have limited insurance coverage for our production facilities and equipment. There is no assurance that our insurance policies will provide sufficient compensation for all potential losses which may arise from damages to our production facilities and equipment. In addition, we may incur property damages arising from production accidents, fire or natural disasters. Our insurance coverage may be insufficient to cover such losses. In the event of a loss in excess of our insured limits or an uninsured loss, our business, financial condition and results of operations could be materially and adversely affected.

Historical advancing activities

For the year ended 31 December 2009, Baoying Renheng provided advances of RMB2,120,000 to Longtai. Details of such advancing activities are set out in the sub-paragraph headed “Financial assistance by our Group to Longtai” under the paragraph headed “Discontinued connected transactions” in the section headed “Connected transactions” in this prospectus. According to the PRC Legal Advisers, any advancing activities between enterprises established in PRC are in breach of 貸款通則 (Loan Regulations) and are subject to the possible penalty imposed by the PBOC of a fine equivalent to 1 to 5 times of the income generated from such advances. The advances made to Longtai by Baoying Renheng were interest free and were fully settled by the year ended 31 December 2010. However, if the relevant PRC laws and regulations change in the future and additional fine, penalty or administrative action is imposed upon or initiated against Baoying Renheng for such historical advancing activities, the operations and financial condition of the Group may be adversely affected.

Future dividend policy

During the Track Record Period and up to the Latest Practicable Date, save for the intra-group dividend of RMB9,932,359.61 declared to Renheng Tech from Baoying Renheng, we did not declare any dividends. We will review our decision to pay dividends taking into consideration a number of factors such as the results of our operations, capital expenditure requirements, our financial position and other factors as we may deem appropriate. Any declaration and payment of dividends will be subject to our memorandum of association and Articles of Association and the Companies Law. There is no assurance that we will pay any dividend on the Shares in the future.

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Failure to implement our future plans

Our future plans have been formulated based on various assumptions as set out in the paragraph headed “Bases and assumptions” under the section headed “Future plans and prospects” in this prospectus. These assumptions are inherently subjective. Should the facts materially deviate from these assumptions, we may not achieve our implementation plans within the scheduled time, or at all.

Uncertainties with respect to the development of our hot stamped foil trading business

On 23 December 2010, we entered into a contract with an Independent Third Party, which was engaged in the sale of packaging material products, to supply hot stamped foil used in cigarette packaging. The revenue derived from the sale of hot stamped foil represented a minor portion of approximately 1.8% of our revenue for the year ended 31 December 2010 and 3.5% of our revenue for the six months ended 30 June 2011. It is not our current intention to establish this trading business as part of our core business. As at the Latest Practicable Date, the hot stamped foil trading business was only at an infancy stage and we did not have any concrete plan regarding the development of this new business. There is no assurance that the hot stamped foil trading business will generate income for our Group in the future.

Our tobacco machinery products have long average replacement cycle

Our Company estimates that the average replacement cycle of our tobacco machinery products is around 8 years, provided that regular inspections and maintenance of the machinery are performed by our customers. While we may from time to time derive revenue from our existing customers by providing maintenance and overhaul services for their machinery products, there is no assurance that we can derive revenue from our existing end customer base through sale of tobacco machinery products as these customers’ needs for product replacement may be low. Furthermore, given the fact that our Group only commenced the manufacturing of tobacco machinery products since November 2001, we do not have a long operating history as compared to the replacement cycle of our products that enables us to ascertain whether we will obtain repeating orders from our existing customers or whether they will select our products for replacement in the future. If our Group is not able to acquire new customers for our tobacco machinery products or develop new products which fulfill the evolving technical and capacity requirements of our new and existing customers, the growth of our turnover from sale of tobacco machinery products may be restricted and as a result our Group’s financial performance may be adversely affected.

RISKS RELATING TO THE INDUSTRY

Competition from other tobacco machinery manufacturers

Competition in the PRC catalogued special-purpose tobacco machinery industry is relatively moderate due to a limited number of participants. All manufacturers engaging in the sale and production of catalogued special-purpose tobacco machinery have to obtain the Tobacco Production Licence. According to the China Tobacco Year Book 2009 published by STMA in December 2010, as at the end 2009, there were 34 tobacco machinery manufacturers which have obtained the Tobacco Production Licence. To the best of our Directors’ knowledge, information and belief, the number of

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competitors which are currently permitted to engage in the manufacture of casing and flavouring system, PF system and PP system are 6, 3 and 3 respectively. There is no assurance that our current and potential competitors will not offer more technologically advanced products, or adapt more quickly to the evolving market requirements. In the event that we are unable to keep abreast with the technological developments or changing market preferences, or maintain our competitiveness against other industry players, our financial results may be adversely affected.

Enforcement of tobacco control regulations in the PRC

The PRC government has promulgated and will continue to promulgate a series of tobacco control regulations. Pursuant to 公共場所衛生管理條例實施細則 (Implementation Rules on the Administrative Regulation of Public Place Sanitation) which was promulgated on 11 March 1991 and implemented on 1 June 1991 by 中華人民共和國衛生部 (Ministry of Health of the PRC), smoking in 14 public indoor places including, among others, theatres, ballrooms, game rooms, gymnasiums, libraries, museums and shops is prohibited. The new Implementation Rules on the Administrative Regulation of Public Place Sanitation which was promulgated on 10 March 2011 and implemented on 1 May 2011 provides that smoking in 28 public indoor places including, among others, hotels, restaurants, bars, theatres, game rooms, parks, exhibition halls, waiting rooms and public transports as set out in 公共場所衛生管理條例 (Administrative Regulation of Public Place Sanitation) is prohibited. As the smoking of cigarettes is harmful to health, the PRC government may introduce stricter controls and measures to discourage people from smoking in the PRC. If more stringent regulations and measures are implemented in the future, the consumption of tobacco-related products in the PRC may be adversely affected and the revenue generated by domestic cigarette manufacturers may therefore decrease. Under such circumstances, the domestic cigarette manufacturers may reduce their demand for our tobacco machinery, and our financial position may be adversely affected.

Effect of change in demand of tobacco products resulting from health hazard awareness and social advocacy for tobacco control

As a result of various media coverage and publication of health researches on smoking from organisations such as the World Health Organization, public awareness of the health hazards associated with tobacco consumption has emerged. Moreover, there exists public health advocacy for tobacco control in the PRC. These may adversely affect the consumption and demand of tobacco-related products and the revenue generated by domestic cigarette manufacturers may therefore decrease. Under such circumstances, domestic cigarette manufacturers may reduce their demand for our tobacco machinery and our financial position may be materially affected.

Effect of changes in the PRC laws, rules and regulations regarding catalogued special-purpose tobacco machinery industry

We, as one of the catalogued special-purpose tobacco machinery manufacturers in the PRC, shall be inspected and supervised by STMA and local tobacco monopoly authorities. Our operation requires several government approvals and is subject to the laws, rules and regulations promulgated by 國家發展和改革委員會 (National Development and Reform Commission) and STMA. Details of the relevant PRC laws, rules and regulations applicable to catalogued special-purpose tobacco machinery

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manufacturers are set out in the section headed “Regulatory overview” in this prospectus. There can be no assurance that the PRC government will not impose additional or more stringent laws, rules or regulations regarding the catalogued special-purpose tobacco machinery industry, compliance with which may cause us to incur significant extra costs, and we may be unable to pass such costs on to our customers. Any change in the scope or application of these laws, rules, regulations or approvals may disrupt our business operation and adversely affect our results of operation.

RISKS RELATING TO THE PRC

Effect of changes in the PRC economic, political and social conditions and government policies

The PRC economy differs from the economies of most developed countries in many respects, including the extent of structure, government involvement, level of development, growth rate, control of foreign exchange, capital reinvestment, allocation of resources, and rate of inflation. The economy of the PRC has been transitioning from a planned economy to a more market-oriented economy. In the recent years, the PRC government has implemented measures emphasising market forces for economic reform, the reduction of state ownership of productive assets and the establishment of sound corporate governance in business enterprises. However, a large portion of productive assets in the PRC are still state-owned. The PRC government also continues to play a significant role in regulating industrial development, the allocation of resources, production, pricing and management, and there can be no assurance that the PRC government will continue to pursue a consistent policy of economic reform.

Substantially all of our operations are conducted in the PRC and all of our revenues are sourced from the PRC. Accordingly, our business, financial condition and results of operations could be adversely impacted by changes in economic, political and social developments and conditions in the PRC and the policies adopted by the PRC government.

Our financial condition and results of operations could also be adversely affected by changes in measures introduced to control inflation, changes in the rate or method of taxation, the imposition of additional restrictions on currency conversion, the imposition of additional import restrictions and other state-driven changes. Moreover, although the PRC economy has grown significantly in recent years, we cannot assure you that the economy will continue to grow, or that its growth will be steady or occur in geographical regions or economic sectors from which we benefit. A downturn in the PRC’s economic growth or a decline in its economic condition may have a material adverse effect on our business, financial condition and results of operations.

Uncertainties with respect to the PRC legal system

The PRC legal system is a civil law system based on written statutes. Unlike in the common law system, prior court decisions may be cited for reference but have limited precedential value. Since 1979, PRC legislation and regulations have significantly enhanced the protections afforded to various forms of foreign investments in the PRC. We conduct all of our business through our subsidiary established in the PRC, Baoying Renheng. This subsidiary is generally subject to laws and regulations applicable to foreign investment in the PRC and, in particular, laws applicable to wholly foreign-owned enterprises. In addition, our offshore holding companies and certain transactions between them may be subject

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to various PRC laws and regulations. However, since these laws and regulations are relatively new and the PRC legal system continues to rapidly evolve, the interpretations of many laws, regulations and rules are not always uniform, and enforcement of these laws, regulations and rules involve uncertainties, which may limit legal protections available to us and could subject us to unexpected liabilities. However, since PRC administrative and court authorities have significant discretion in interpreting and implementing statutory and contractual terms, it may be more difficult to evaluate the outcome of administrative and court proceedings and the level of legal protection we enjoy than in more developed legal systems. Such uncertainties, including the inability to enforce our contracts, could have a material adverse effect on our operations. Furthermore, intellectual property rights and confidentiality protections in the PRC may not be as effective as in other countries. Accordingly, we cannot predict the effect of future developments in the PRC legal system, particularly with regard to the PRC tobacco industry and tobacco machinery industry, including the promulgation of new laws, changes to existing laws or the interpretation or enforcement thereof, or the pre-emption of local regulations by national laws. These uncertainties could limit the legal protections available to us and other foreign investors, including you. In addition, any litigation in the PRC may be protracted and result in substantial costs and diversion of our resources and management attention.

If the favourable tax treatments that we currently receive are altered or eliminated, our results of operations may be adversely affected

Our subsidiary incorporated in the PRC is subject to PRC enterprise income tax and value-added tax. As advised by the PRC Legal Advisers, in accordance with the relevant income tax laws and regulations of the PRC, Baoying Renheng was exempted from enterprise income tax for two years commencing from 2002, and was entitled to a 50% reduction in its enterprise income tax for the subsequent three years. Therefore, from 1 January 2004 to 31 December 2006, the applicable enterprise income tax rate for Baoying Renheng was 15%. With effect from 1 January 2008, Baoying Renheng is subject to an enterprise income tax rate of 25% pursuant to the EIT Law. Baoying Renheng enjoyed the preferential treatments granted by the People's Government of Baoying pursuant to which (i) Baoying Renheng would receive a refund of 50% of enterprise income tax in respect to the portion received by the People's Government of Baoying, which would be equivalent to 16% of the total enterprise income tax paid for the respective years, for a period of 5 years from 1 January 2007 to 31 December 2011; and (ii) Baoying Renheng would receive a 12.5% refund of the excess of the value-added tax paid by Baoying Renheng over the value-added tax paid by Baoying Radio Factory in 2000, for an indefinite period of time. When the preferential tax treatments currently enjoyed by Baoying Renheng become invalid, or are altered or eliminated, our results of operations may be adversely affected.

PRC regulations on loans to and direct investment by offshore holding companies in PRC entities may delay or prevent us from using the proceeds from the Placing to make loans or additional capital contributions to our PRC subsidiary

As an offshore holding company of our PRC subsidiary, we may make loans to our PRC subsidiary, or we may make additional capital contributions to our PRC subsidiary. Any loans to our PRC subsidiary are subject to PRC regulations and foreign exchange loan registrations. For example, loans by us to our PRC subsidiary to finance its activities cannot exceed statutory limits and must be registered with the SAFE or its local counterpart. We may also determine to finance our PRC

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subsidiary by means of capital contributions. These capital contributions must be approved by the 中華人民共和國商務部 (Ministry of Commerce of the PRC) or its local counterpart. We cannot assure you that we can obtain these government registrations or approvals on a timely basis, if at all, with respect to future loans or capital contributions by us to finance our PRC subsidiary. If we fail to receive relevant registrations or approvals, our ability to use the proceeds from the Placing and to capitalise our PRC operations would be negatively affected which would adversely and materially affect our liquidity and our ability to expand our business in the PRC.

Fluctuations in the value of RMB and government control over currency exchange could adversely affect our business, operating results and financial condition

All our revenue and the majority of our expenditures are denominated in RMB, which is currently not a freely convertible currency. In addition, we will require foreign currencies for dividend payment (if any) to our Shareholders. As a result, we are exposed to foreign currency fluctuations. In the PRC, since 1994, the conversion of RMB into foreign currencies, including HK\$, has been based on rates set by the PBOC. The PRC Government has, with effect from 21 July 2005, reformed the exchange rate regime by permitting RMB to fluctuate within a narrow and managed band based on market supply and demand with reference to a basket of currencies. The PRC Government has since made further adjustments to the exchange rate system. Any appreciation of RMB may result in the decrease in the value of our foreign currency-denominated assets, including the net proceeds from the Placing. Over the years, the PRC Government has significantly reduced its control over routine foreign exchange transactions under current accounts items, including trade and service-related foreign exchange transactions and payment of dividends. However, foreign exchange transactions under capital accounts items continue to be subject to significant foreign exchange controls and require the approval of, or registration with, SAFE. Under our current group structure, our Company's income is derived principally from dividend payments from our only subsidiary located in the PRC, Baoying Renheng. Shortages in foreign currency may restrict the ability of Baoying Renheng to remit sufficient foreign currency to pay dividends or other payments to us, or otherwise satisfy its foreign currency-denominated obligations.

In addition, under the current foreign exchange regulations in China, subject to the relevant registration at the SAFE, we are able to pay dividends in foreign currencies, without prior approval from the SAFE, by complying with certain procedural requirements. However, there can be no assurance that the current PRC foreign exchange policies regarding debt service and payment of dividends in foreign currencies will continue in the future. Changes in PRC foreign exchange policies might have a negative impact on our ability to service our foreign currency-denominated indebtedness and to distribute dividends to our Shareholders in foreign currencies.

Enforcement of the labour contract law and other labour-related regulations in the PRC

A new labour contract law became effective on 1 January 2008 in the PRC. It imposes more stringent requirements on employers with respect to entering into fixed term employment contracts, hiring temporary employees and dismissing employees. In addition, under the newly promulgated Regulations on Paid Annual Leave for Employees, which became effective on 1 January 2008, each employee who has served more than one year for an employer is entitled to a paid vacation ranging

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from 5 to 15 days, depending on length of service. Employees who waive such vacation time at the request of employers must be compensated for three times their regular salaries for each waived vacation day. As a result of the PRC law, our labour costs have increased. We cannot assure you that any disputes, work stoppages or strikes will not arise in the future. Furthermore, there can be no assurance that there will be additional or new labour laws, rules and regulations in the PRC, which may lead to potential increases in our labour cost. In such events, our business, financial condition or results of operations may be materially and adversely affected.

Significant uncertainties under the new enterprise income tax law relating to our PRC enterprise income tax liabilities

Under the new enterprise income tax law effective on 1 January 2008, the profits of a foreign invested enterprise arising in 2008 and onwards which are distributed to its immediate holding company outside the PRC will be subject to a withholding tax rate of 10%. Pursuant to a special arrangement between Hong Kong and the PRC, such rate is lowered to 5% if a Hong Kong resident enterprise owns over 25% of the PRC company. According to 關於印發《非居民享受稅收協定待遇管理辦法(試行)》的通知 (the Circular of State Administration of Taxation on Printing and Issuing the Administrative Measures for Non-resident Individuals and Enterprises to Enjoy the Treatment Under Taxation Treaties), which became effective on 1 October 2009, the 5% tax rate does not automatically apply. Approvals from competent local tax authorities are required before an enterprise can enjoy the relevant tax treatments relating to dividends under relevant taxation treaties. During the Track Record Period, we have accrued provisions of approximately HK\$593,000, at the withholding tax rate of 5%, nil and nil respectively. In addition, according to a tax circular issued by the State Administration of Taxation in February 2009, if the main purpose of an offshore arrangement is to obtain a preferential tax treatment, the PRC tax authorities have the discretion to adjust the preferential tax rate enjoyed by the relevant offshore entity.

Although our Company is a Cayman Islands company and the equity interests of our PRC subsidiary Baoying Renheng are directly held by our subsidiary in Hong Kong, Renheng Tech, the PRC tax authorities may regard the main purpose of Renheng Tech as obtaining a lower withholding tax rate of 5%. As a result, even if we have obtained such approval regarding a lower withholding tax rate, it is possible that the PRC tax authorities could levy a higher withholding tax rate to dividends received by Renheng Tech from Baoying Renheng.

Uncertainties regarding the regulatory requirements on statutory reserves

We are a holding company incorporated in the Cayman Islands and we operate our core business through our subsidiary in China, Baoying Renheng. Therefore, the availability of funds for us to pay dividends to our Shareholders depends upon dividends received from Baoying Renheng. The PRC laws require foreign invested enterprises to set aside part of their net profit as statutory reserves. These statutory reserves are not available for distribution as cash dividends. Therefore, these restrictions on the availability and usage of our major source of funding may adversely impact our ability to pay dividends to our Shareholders.

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Natural disasters, acts of war, political unrest and epidemics

Natural disasters, acts of war, political unrest and epidemics, which are beyond our control, may adversely affect the economy, infrastructure and livelihood of the people of China. Some cities in China are particularly susceptible to floods, earthquakes, sandstorms and droughts. Political unrest, acts of war and terrorists attacks may cause damage or disruption to us, our employees or our facilities. The potential for war or terrorists attacks may also cause uncertainty and cause our business to suffer in ways that we cannot currently predict. In addition, certain Asian countries, including China, have encountered epidemics such as severe acute respiratory syndrome, or incidents of the avian flu. Past occurrences of epidemics have caused different degrees of damage to the national and local economies in China. A recurrence of an outbreak of severe acute respiratory syndrome, avian flu, influenza A (H5N1) (swine flu) or any other similar epidemic could cause a slowdown in the levels of economic activity generally. Our business, revenue, financial condition and results of operations could be materially and adversely affected by such disasters.

Tightening of credit in the PRC

During the Track Record Period, all of our revenue was derived from sales in the PRC. The end customers of our products and services are generally domestic cigarette manufacturers and tobacco redrying factories in the PRC. The demand for our tobacco machinery products depends significantly on the level of capital spending by such cigarette manufacturers and tobacco redrying factories. The tightening of credit in the PRC may restrict the ability of our Group and our end customers to obtain financing from financial institutions in the PRC on commercially reasonable terms, or at all, which could materially and adversely affect the future operation, business and financial position of both our Company and our end customers.

RISKS RELATING TO THE PLACING

Termination of the Underwriting Agreement

Prospective investors of the Placing Shares should note that Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) is entitled to terminate the Underwriting Agreement by giving notice in writing to our Company upon the occurrence of any of the events stated in the subparagraph headed “Grounds for termination” under the paragraph headed “Underwriting arrangements” the section headed “Underwriting” in this prospectus at any time prior to 8:00 a.m. (Hong Kong time) on the Listing Date. Such events include, without limitation, acts of government, strikes, lockout, fire, explosion, flooding, civil commotion, acts of war or acts of God or accident.

No prior public market for the Shares

The Listing is by way of the Placing and the Shares have not been listed or quoted on any stock exchange or open market before completion of the Placing. There can be no assurance that an active and a liquid market for the Shares will develop or be sustained on GEM upon Listing. In addition, the market price of the Shares to be traded on GEM may differ from the Placing Price and investors should not treat the Placing Price as an indicator of the market price of the Shares to be traded on GEM. Prices for the Shares will be determined in the market place and may be influenced by various factors, including liquidity of the Shares, investors’ perceptions of us and the industry

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in which we operate and the general economic and market conditions in Hong Kong and the PRC. Accordingly, we cannot predict whether an active or liquid trading market for the Shares will develop or be sustained.

Trading price and trading volume of the Shares may be volatile

The price and trading volume of the Shares may be volatile. Factors such as variations in our revenues, earnings and cash flow, strategic alliances or acquisitions, industrial or environmental accidents suffered by us, loss of key personnel, changes in ratings by financial analysts and credit rating agencies, litigation or fluctuations in the market prices for the products or the raw materials could cause large and sudden changes in the volume and price at which the Shares will trade. In addition, significant price and volume fluctuations that are not related to our operating performance may sometimes occur. These fluctuations may also materially and adversely affect the market price of the Shares.

Dilution of Shareholders' equity interests as a result of additional equity fund raising or the exercise of the share options granted by our Company

One of the benefits to our Company upon Listing is the access to capital markets and we may raise additional funds to finance future expansion of our business or operations or acquisitions. We will comply with Rule 17.29 of the GEM Listing Rules, which specifies that no further Shares or securities convertible into equity securities of the Company (subject to certain exceptions) may be issued or form the subject of any agreement to be issued within six months from the Listing Date. Upon expiry of such six-month period, we may raise additional funds by way of issue of new equity or equity-linked securities of our Company and such fund raising exercises may not be conducted on a pro-rata basis to existing Shareholders. As such, the shareholding of the then Shareholders may be reduced or diluted and subject to the terms of the issue of the new securities, and the new securities may confer rights and privileges that have priority over those conferred by the issued Shares.

Our Group has conditionally adopted the Pre-IPO Share Option Scheme under which options entitling the holders thereof to subscribe for an aggregate of 1,300,000 Shares have been granted. Save for the options which have been granted as of the Latest Practicable Date, no further option will be granted under the Pre-IPO Share Option Scheme on or after the Listing Date. Assuming all options granted under the Pre-IPO Share Option Scheme had been exercised in full on 1 January 2010 and 200,000,000 Shares to be in issue immediately following completion of the Capitalisation Issue and the Placing had been in issue throughout the year ended 31 December 2010, there would be a dilution effect of approximately 0.7% on the earnings per Share for the year ended 31 December 2010 from approximately 9.97 cents to approximately 9.90 cents. The options granted under the Pre-IPO Share Option Scheme represent 0.65% of the enlarged issued share capital of our Company immediately following completion of the Capitalisation Issue and the Placing. If all the options are exercised, there would be a dilution effect on the shareholding of our Shareholders of 0.65%.

Our Company has also conditionally adopted the Share Option Scheme but no option has been or will be granted thereunder prior to the Listing Date. Any exercise of any options to be granted under the Share Option Scheme in the future and allotment and issuance of Shares thereunder would result in the reduction in the shareholding of the Shareholders in our Company and may result in a dilution in the earnings per Share and net asset value per Share.

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The laws of the Cayman Islands relating to the protection of interest of minority shareholders may be different from those in Hong Kong

Our corporate affairs are governed by our memorandum and articles of association, the Companies Law and common law of the Cayman Islands. The laws of the Cayman Islands relating to the protection of the interests of minority shareholders may differ in some respects from those established under statutes or judicial precedent in existence in Hong Kong. These differences may mean that our minority Shareholders may have different protections that they would have under the laws of Hong Kong. A summary of Cayman Islands law on the protection of minority shareholders is set out in the section headed “Protection of minorities” in Appendix IV to this prospectus.

RISKS RELATING TO THE PROSPECTUS

Potential unreliability of facts and statistics with respect to information obtained from various official government sources

This prospectus includes certain statistics and facts that have been extracted from government official sources and publications or other sources. We believe the sources of these statistics and facts are appropriate for such statistics and facts and have taken reasonable care in extracting and reproducing such statistics and facts. There is no ground for us to believe that such statistics and facts are false or misleading or that any fact has been omitted that would render such statistics and facts false or misleading. The statistics and facts from these sources have not been independently verified by our Company, Shenyin Wanguo (in any of its capacities as the Sponsor, the Lead Manager or the Underwriter), any of their respective directors or any other party involved in the Placing and therefore, none of them makes no representation as to the accuracy of these statistics and facts. Accordingly, such statistics and facts should not be unduly relied upon.

Potential unreliability of facts and statistics with respect to information contained in the press articles or other media regarding our Company and the Placing

We strongly caution you not to place any reliance on any information contained in press articles or other media regarding us and the Placing. We have not authorised the disclosure of any information in the press or media. We do not accept any responsibility for any such press or media coverage or the accuracy or completeness of any such information. We make no representation as to the appropriateness, accuracy, completeness or reliability of any such information or publication. To the extent that any such information is inconsistent or conflicts with the information contained in this prospectus, we disclaim responsibility for it and you should not rely on any such information.

Forward-looking statements

This prospectus contains certain forward-looking statements relating to the plans, objectives, expectations and intentions of our Directors. Such forward-looking statements are based on numerous assumptions as to our present and future business strategies and the development of the environment in which we operate. These statements involve known and unknown risks, uncertainties and other factors which may cause our actual financial results, performance or achievements to be materially different from the anticipated financial results, performance or achievements expressed or implied by these statements. Our actual financial results, performance or achievements may differ materially from those discussed in this prospectus. Investors should not place undue reliance on such forward looking information.

INFORMATION ABOUT THIS PROSPECTUS AND THE PLACING

DIRECTORS' RESPONSIBILITY FOR THE CONTENTS OF THIS PROSPECTUS

This prospectus, for which our Directors collectively and individually accept full responsibility, includes particulars given in compliance with the Companies Ordinance and the GEM Listing Rules for the purpose of giving information with regard to our Company. Our Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief, the information contained in this prospectus is accurate and complete in all material respects and not misleading or deceptive and there are no other matters the omission of which would make any statement in this prospectus misleading.

Printed copies of this prospectus are available, for information purposes only, at the principal place of business of Shenyin Wanguo at 28/F., Citibank Tower, Citibank Plaza, 3 Garden Road, Hong Kong during normal office hours from 9:00 a.m. to 5:00 p.m. from 28 October 2011 up to and including 9 November 2011 (both dates inclusive, but excluding any Saturday and Sunday).

PLACING SHARES ARE FULLY UNDERWRITTEN

This prospectus set out the terms and conditions of the Placing.

This prospectus is published solely in connection with the Placing, which is sponsored by the Sponsor and managed by the Lead Manager and is fully underwritten by the Underwriter (subject to the terms and conditions of the Underwriting Agreement). Further information about the Underwriter and the underwriting arrangements is contained in the section headed "Underwriting" in this prospectus.

RESTRICTIONS ON SALE OF THE PLACING SHARES

Each person acquiring the Placing Shares will be required, and is deemed by his acquisition of the Placing Shares, to confirm that he is aware of the restrictions on offers and sales of the Placing Shares described in this prospectus.

As at the Latest Practicable Date, no action has been taken in any jurisdiction other than Hong Kong to permit the offering of the Placing Shares or the distribution of this prospectus in any jurisdiction other than Hong Kong. Accordingly, this prospectus may not be used for the purposes of, and does not constitute, an offer or invitation in any jurisdiction or in any circumstance in which such offer or invitation is not authorised or to any person to whom it is unlawful to make an unauthorised offer or invitation. No invitation may be made to the public in the Cayman Islands to subscribe for or purchase any of the Placing Shares.

The Placing Shares are offered for subscription solely on the basis of the information contained, and the representations made in this prospectus. No person is authorised in connection with the Placing to give any information, or to make any representation, not contained in this prospectus, and any information or representation not contained herein must not be relied upon as having been authorised by our Company, Shenyin Wanguo (in any of its capacities as the Sponsor, the Lead Manager or the Underwriter), any of their respective directors or employees or any other persons involved in the Placing.

INFORMATION ABOUT THIS PROSPECTUS AND THE PLACING

APPLICATION OF LISTING ON GEM

Our Company satisfies the requirements relating to continuity of ownership and control throughout the full financial year immediately preceding the Latest Practicable Date and up until the Listing Date under Rule 11.12A(2) of the GEM Listing Rules.

Our Company has applied to the Stock Exchange for the listing of, and permission to deal in, the Shares in issue and to be issued pursuant to the Capitalisation Issue and the Placing and any new Shares which may be allotted and issued pursuant to the exercise of options that have been granted under the Pre-IPO Share Option Scheme or may be granted under the Share Option Scheme and as otherwise described herein. Pursuant to Rule 11.23(7) of the GEM Listing Rules, at least 25% of the total issued share capital of the Company must at all times be held by the public. A total of 50,000,000 Placing Shares representing 25% of the enlarged issued share capital of our Company will be in the hands of the public immediately following completion of the Capitalisation Issue and the Placing, and upon Listing (without taking into account of any new Shares which may be allotted and issued pursuant to the exercise of options that have been granted under the Pre-IPO Share Option Scheme or may be granted under the Share Option Scheme).

No part of our Company's share or loan capital is listed or dealt in on any other stock exchange. As at the Latest Practicable Date, our Company was not seeking or proposing to seek a listing of, or permission to deal in, any part of its share or loan capital on any other stock exchange other than the Stock Exchange.

The Shares are freely transferable. Under Section 44B(1) of the Companies Ordinance, any allotment or transfer made in respect of any placing of the Placing Shares will be void if permission for the listing of, and dealing in, the Shares on GEM has been refused before the expiration of three weeks from the date of closing of the Placing or such longer period (not exceeding six weeks) as may, within the said three weeks, be notified to our Company by or on behalf of the Stock Exchange.

PROFESSIONAL TAX ADVICE RECOMMENDED

Potential investors for the Placing Shares are recommended to consult their professional advisers if they are in doubt as to the taxation implications of the subscription for, holding, purchase, disposal of or dealing in the Shares or exercising their rights thereunder.

It is emphasised that none of our Company, our Directors, Shenyin Wanguo (in the respective capacity as the Sponsor, the Lead Manager or the Underwriter) and their respective directors or employees or any other persons involved in the Placing accepts responsibility for any tax effects on, or liability of, holders of Shares resulting from the subscription for, holding, purchase, disposal of or dealing in the Shares.

STAMP DUTY

All the Shares will be registered on the branch register of members of our Company in Hong Kong. Dealings in the Shares registered on our Company's branch register of members maintained in Hong Kong will be subject to Hong Kong stamp duty. Dealings in the Shares will not be subject to the Cayman Islands stamp duty.

INFORMATION ABOUT THIS PROSPECTUS AND THE PLACING

STRUCTURE AND CONDITIONS OF THE PLACING

Details of the structure and conditions of the Placing are set out in the section headed “Structure and conditions of the Placing” of this prospectus.

SHARES WILL BE ELIGIBLE FOR ADMISSION INTO CCASS

Subject to the approval of the listing of, and permission to deal in, the Shares in issue and to be issued as mentioned in this prospectus on GEM and if our Company complies with the stock admission requirements of HKSCC, the Shares will be accepted as eligible securities by HKSCC for deposit, clearance and settlement in CCASS with effect from the Listing Date, or on any other date as may be determined by HKSCC. Settlement of transactions between participants of the Stock Exchange is required to take place in CCASS on the second business day after any trading day. Investors should seek the advice of their stockbroker or other professional adviser for details of those settlement arrangements as such arrangements will affect their rights and interests.

All activities under CCASS are subject to the General Rules of CCASS and CCASS Operational Procedures in effect from time to time.

All necessary arrangements have been made for the Shares to be admitted into CCASS.

COMMENCEMENT OF DEALING IN THE SHARES

Dealings in the Shares are expected to commence at 9:00 a.m. on Friday, 18 November 2011. Shares will be traded in board lots of 2,000 Shares each.

DIRECTORS AND PARTIES INVOLVED IN THE PLACING

DIRECTORS

Name	Address	Nationality
Executive Directors		
Mr. Wei Sheng Peng (魏勝鵬)	41A, Tower 3, The Legend 23 Tai Hang Drive Hong Kong	Singaporean
Ms. Liu Li (劉利)	41A, Tower 3, The Legend 23 Tai Hang Drive Hong Kong	Chinese
Mr. Sun Zhaohui (孫朝暉)	Apt Blk 116 Bukit Batok West Avenue 6 #12-230 Singapore 650116	Singaporean
Independent non-executive Directors		
Mr. Tam Yuk Sang, Sammy (譚旭生)	House 5, Palm Cove Villa 25 Ng Fai Tin Clear Water Bay New Territories Hong Kong	Chinese
Mr. Wong Yiu Kit (黃耀傑)	Room 1, 3/F., Block 40 Heng Fa Chuen 100 Shing Tai Road Hong Kong	Chinese
Mr. Kong Hing Ki (江興琪)	Flat H, 9th Floor Far East Mansion 5 Middle Road Tsimshatsui Kowloon Hong Kong	Chinese

DIRECTORS AND PARTIES INVOLVED IN THE PLACING

PARTIES INVOLVED IN THIS PLACING

Sponsor and Lead Manager	Shenyin Wanguo Capital (H.K.) Limited 28/F., Citibank Tower Citibank Plaza 3 Garden Road Central Hong Kong
Legal advisers to the Company	<i>As to Hong Kong law</i> Louis K.Y. Pau & Company, Solicitors 4/F., The Chinese Club Building 21-22 Connaught Road Central Hong Kong <i>As to Cayman Islands law</i> Maples and Calder 53/F., The Center 99 Queen's Road Central Hong Kong <i>As to PRC law</i> Grandall Legal Group (Shenzhen) 22/F. & 24/F., Shenzhen Special Zone Press Tower 6008 Shennan Blvd. Shenzhen PRC
Legal advisers to the Sponsor and the Underwriter	Li & Partners 22/F., World-Wide House Central Hong Kong
Auditors & reporting accountants	Deloitte Touche Tohmatsu Certified Public Accountants 35/F., One Pacific Place 88 Queensway Hong Kong
Property valuer	Greater China Appraisal Limited Room 2703 Shui On Centre 6-8 Harbour Road, Wanchai Hong Kong

CORPORATE INFORMATION

Registered office	PO Box 309 Ugland House Grand Cayman, KY1-1104 Cayman Islands
Head office and principal place of business in Hong Kong	Room 1303, 13/F. Keen Hung Commercial Building 80 Queen's Road East Wanchai Hong Kong
Compliance officer	Mr. Sun Zhaohui (孫朝暉)
Company secretary	Mr. Ho Pui Lam Joseph (何沛霖) <i>Certified Public Accountants</i>
Authorised representatives	Ms. Liu Li (劉利) 41A, Tower 3, The Legend 23 Tai Hang Drive Hong Kong Mr. Ho Pui Lam Joseph (何沛霖) Flat D, 5/F. Ka On Building 27-29 Poplar Street Sham Shui Po Kowloon
Compliance adviser	Shenyin Wanguo Capital (H.K.) Limited 28/F., Citibank Tower Citibank Plaza 3 Garden Road Central Hong Kong
Audit committee	Mr. Wong Yiu Kit (黃耀傑) (Chairman) Mr. Tam Yuk Sang, Sammy (譚旭生) Mr. Kong Hing Ki (江興琪)
Remuneration committee	Mr. Kong Hing Ki (江興琪) (Chairman) Mr. Wong Yiu Kit (黃耀傑) Mr. Tam Yuk Sang, Sammy (譚旭生)

CORPORATE INFORMATION

Nomination committee	Mr. Tam Yuk Sang, Sammy (譚旭生) (Chairman) Mr. Wong Yiu Kit (黃耀傑) Mr. Kong Hing Ki (江興琪)
Principal share registrar and transfer office	Butterfield Fulcrum Group (Cayman) Limited Butterfield House, 68 Fort Street, P.O. Box 609 Grand Cayman KY1-1107 Cayman Islands
Hong Kong branch share registrar and transfer office	Tricor Investor Services Limited 26th Floor, Tesbury Centre 28 Queen's Road East Hong Kong
Principal bankers	Bank of China (Hong Kong) Limited United Centre Sub-Branch Shop 1021, United Centre 95 Queensway Hong Kong Industrial and Commercial Bank of China Limited Baoying Sub-Branch 39 Suzhong South Road Baoying County Jiangsu Province PRC China Construction Bank Corporation Baoying Sub-Branch 3 Yeting East Road Baoying County Jiangsu Province PRC Bank of Jiangsu Co., Ltd. Yangzhou Branch 68 Baitian Middle Road Baoying County Jiangsu Province PRC
Website of the Company	www.renhengenterprise.com (information on this website does not form part of this prospectus)

INDUSTRY OVERVIEW

This section contains certain information which is derived, in part, from various official government sources and publicly available sources. Our Directors believe that the sources of such information are appropriate sources for such information and have taken reasonable care in extracting and reproducing such information. Our Directors have no reason to believe that such information is false or misleading or that any fact has been omitted that would render such information false or misleading. The information has not been independently verified by us, Shenyin Wanguo (in any of its capacities as the Sponsor, the Lead Manager or the Underwriter) or any other party involved in the Placing, or their respective directors, officers, employees, advisers and agents. No representation is given as to the accuracy of such information. Accordingly, such information should not be unduly relied upon.

The information in respect of the market position or the market share of our Group is not presented in this prospectus as no official statistics of the tobacco machinery market is available from the relevant government authorities, industry bodies, research agencies and/or other reliable public domain.

TOBACCO INDUSTRY IN THE PRC

A highly regulated industry

China's tobacco industry adopts a system of unified leadership, vertical management and monopolised operation. STMA and CNTC are responsible for the centralised management of "staff, finance, properties, products, supply, distribution, and domestic and foreign trade" of the tobacco industry in the PRC.

The CNTC was founded in December 1983. The State Council issued the Rules on Tobacco Monopoly in September 1983, setting forth the national tobacco monopoly system officially. The STMA was established in January 1984. The Standing Committee of the National People's Congress approved 中華人民共和國煙草專賣法 (the Law of the PRC on Tobacco Monopoly) in June 1991. The State Council issued 中華人民共和國煙草專賣法實施條例 (the Rules for Implementation of the Law of the PRC on Tobacco Monopoly) in July 1997. The issuance and implementation of the laws and regulations further enhance and improve the national tobacco monopoly system. To the best of our Directors' knowledge, information and belief, the industry covered 33 provincial tobacco monopoly administrations and companies, 16 companies, 57 industrial enterprises, over 1,000 commercial enterprises, and companies specialised in leaf tobacco, cigarette selling, cigarette-making machinery, materials, imports and exports, as well as other institutions, with a total force of 510,000 employees as at the Latest Practicable Date.

Consolidation of PRC tobacco industry

According to 國家煙草專賣局關於煙草行業捲煙工業企業組織結構調整的實施意見 (the Opinion of STMA on the Implementation of the Adjustment of Organisational Structure of Cigarette Industrial Enterprises in the Tobacco Industry) issued in May 1998, the tobacco industry in the PRC was too fragmented in view of the large number of small-sized cigarette manufacturers with low production

INDUSTRY OVERVIEW

capacity. A series of reform policies was introduced by STMA to consolidate and integrate small cigarette manufacturers. These policies included the closure of small cigarette factories with annual production volume of less than 100,000 cartons, the merger or reorganisation of factories with annual production volume ranging from 100,000 to 300,000 cartons and developing as well as expanding cigarette factories with annual production volume of more than 300,000 cartons. As a further step to consolidate the tobacco industry, STMA issued 關於捲煙工業跨省聯合重組工作的指導意見 (the Guidance Opinion on the Cross-province Reorganisation of Cigarette Industrial Enterprises) in May 2008. As a result of the consolidation of the tobacco industry, the number of cigarette industrial enterprises in the PRC has been reduced to 30 in 2009.

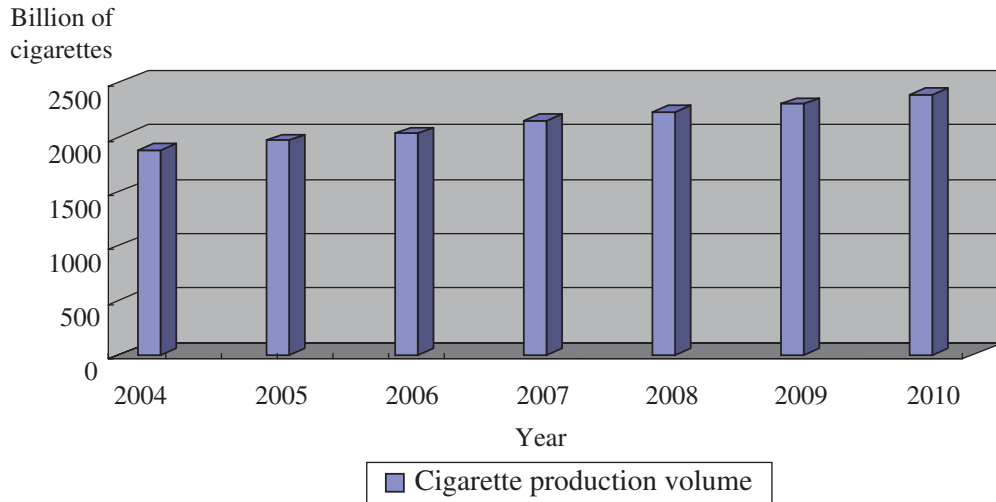
The PRC government has also taken steps to consolidate domestic cigarette brands to strengthen the competitiveness of the Chinese tobacco industry. In August 2004, STMA promulgated 關於印發《捲煙產品百牌號目錄》的通知 (the Notice on Issuing the List of One Hundred Cigarette Brands), pursuant to which STMA aimed to reduce the number of domestic cigarette brands to around 100 in the following 2 to 3 years. In 2007, the total number of domestic cigarette brands was reduced to 173 from 758 in 2002. As a further step to consolidate the PRC tobacco industry, STMA proposed the “532” and “461” strategic plans at the 2010 Annual National Tobacco Work Conference held on 19 January 2010. According to the “532” plan, STMA will put emphasis on building 2 domestic cigarette brands with annual production volume of over 5 million carton boxes, 3 domestic cigarette brands with annual production volume of over 3 million and 5 domestic cigarette brands with annual production volume of over 2 million carton boxes in the next five years. Under the “461” plan, STMA is committed to developing 12 domestic cigarette brands with annual sales revenue surpassing RMB40 billion, including 4 domestic brands with annual sales revenue of over RMB60 billion, and 1 domestic brand with annual sales revenue of over RMB100 billion by the year of 2015.

Size of the cigarette industry in the PRC

The Global Adult Tobacco Survey, a nationally representative household survey published by GTSS in August 2010, indicates that the number of adult smokers in China was approximately 301 million in 2010, representing approximately 28.1% of the total population of China. According to the Atlas, the largest state monopoly is CNTC, with a global cigarette market share of approximately 32.0% in 2007 which exceeded that of any private company. Under the national tobacco monopoly system, total cigarette production in the PRC remained relatively stable in recent years. The total cigarette production volume in China rose from approximately 1,874.4 billion in 2004 to approximately 2,375.3 billion in 2010, representing a CAGR of approximately 4.0%. The chart below sets forth China’s total cigarette production volume between 2004 and 2010.

INDUSTRY OVERVIEW

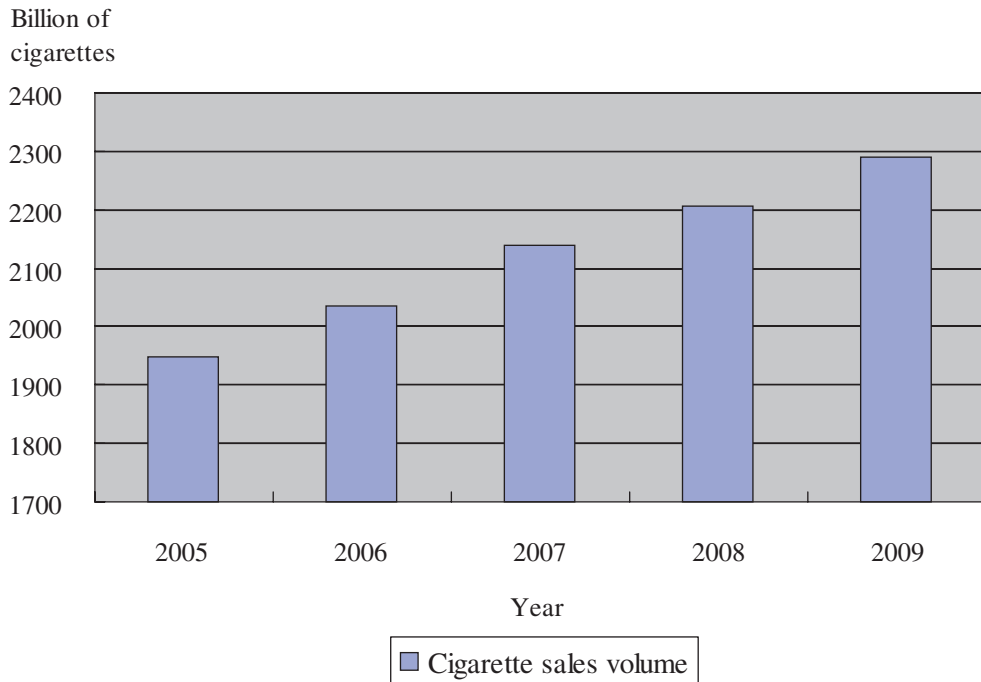
Cigarette production volume



Source: National Bureau of Statistics of China

According to the statistics of the China Tobacco Year Book issued by STMA for 2005 to 2009, the sales volume of cigarettes in the PRC increased at a CAGR of approximately 4.1% from 2005 to 2009. The following chart sets forth the sales volume of cigarettes in the PRC for the periods indicated.

Cigarette sales volume



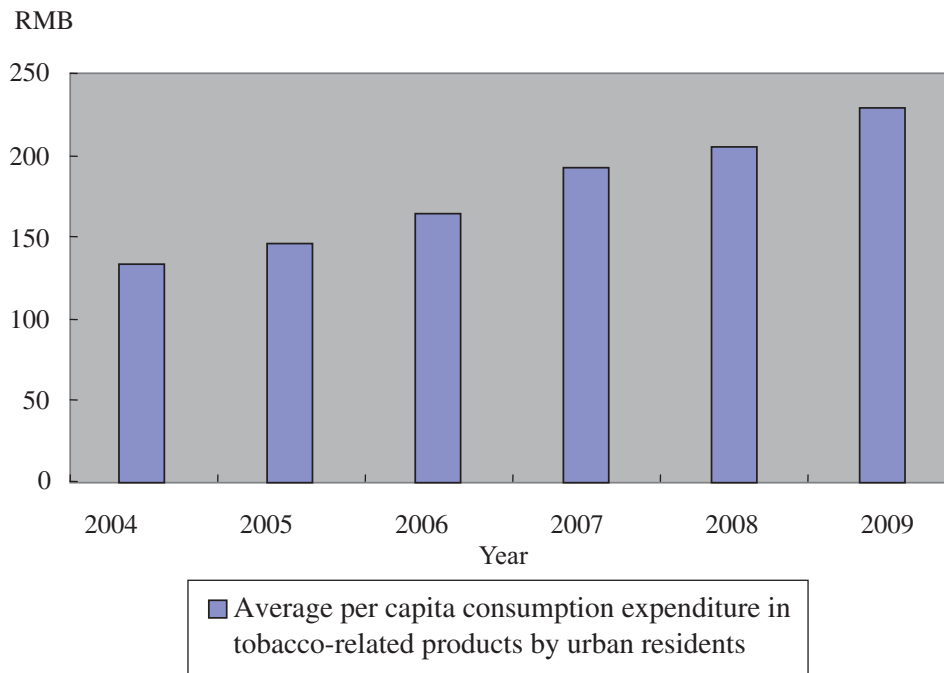
Source: China Tobacco Year Book (2005–2009)

INDUSTRY OVERVIEW

According to the National Bureau of Statistics of China, the average per capita consumption expenditure in tobacco-related products by urban residents in China reached approximately RMB228.5 in 2009, representing a 11.5% increase from approximately RMB205.0 in 2008. During 2004 to 2009, the average per capita consumption expenditure in tobacco-related products by urban residents in PRC grew at a CAGR of approximately 11.3%.

The following chart sets forth the growth of the average per capita consumption expenditure in tobacco-related products by urban residents in China between 2004 and 2009.

**Average per capita consumption expenditure in tobacco-related products
by urban residents in PRC**

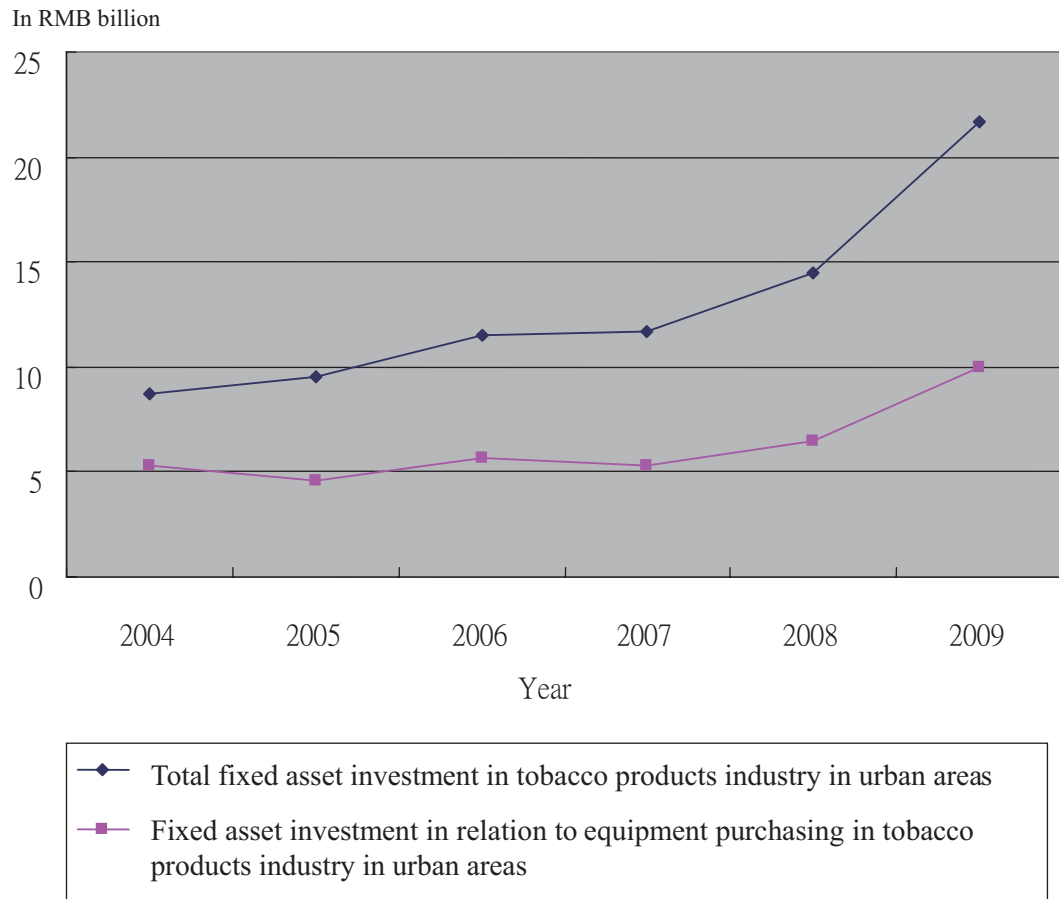


Source: National Bureau of Statistics of China

According to the National Bureau of Statistics of China, fixed asset investment in the tobacco products industry in urban areas (煙草製品業城鎮固定資產投資) grew at a CAGR of approximately 20.1% between 2004 and 2009 from RMB8.7 billion to RMB21.7 billion whilst fixed asset investment in relation to equipment purchasing in the tobacco products industry in urban areas (煙草製品業城鎮固定資產投資—設備、工器具購置) increased at a CAGR of approximately 13.5% from RMB5.3 billion to RMB10.0 billion in the same period.

INDUSTRY OVERVIEW

Fixed asset investment in tobacco-related products industry in urban areas in the PRC



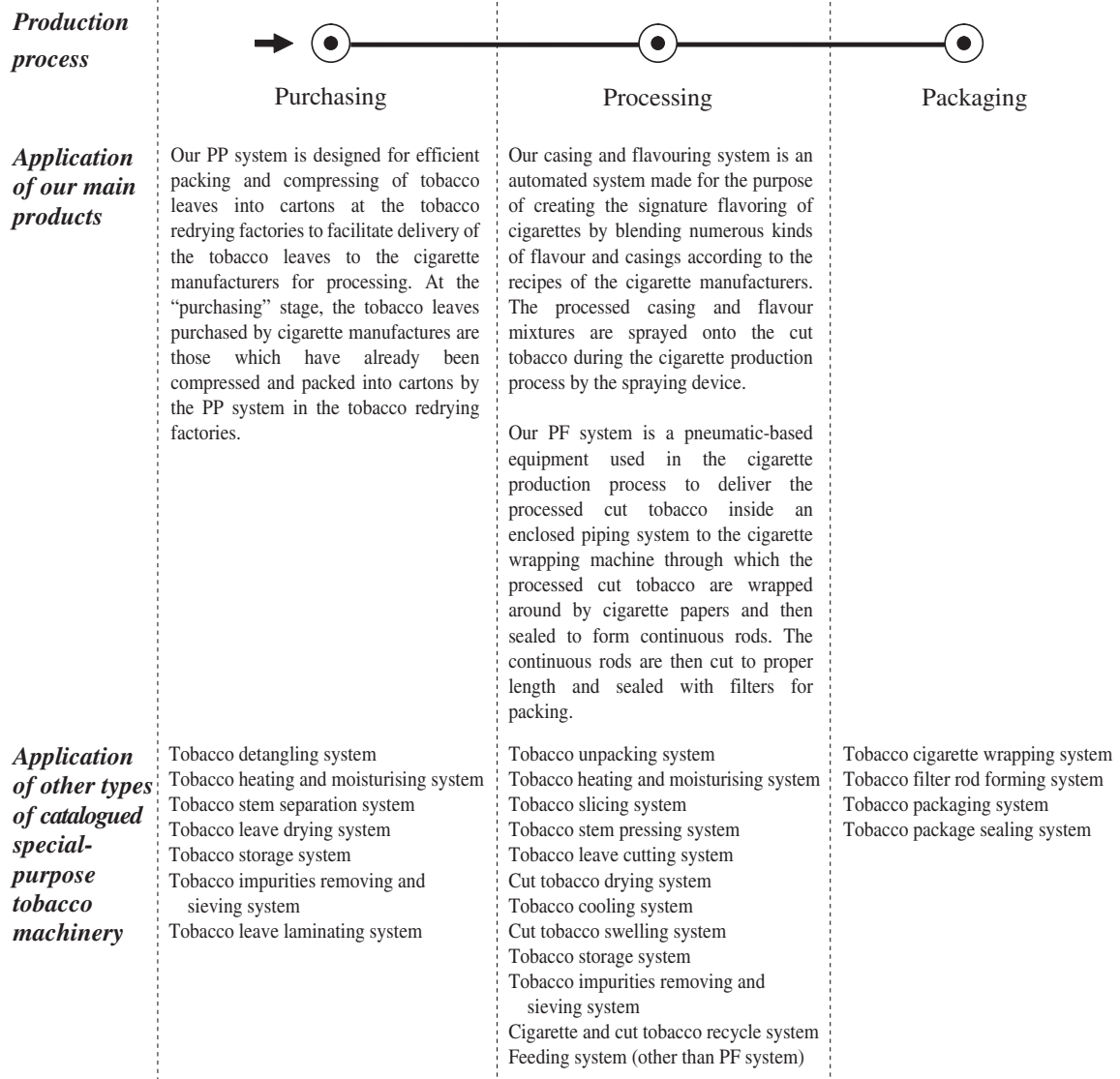
Source: National Bureau of Statistics of China

INDUSTRY OVERVIEW

TOBACCO MACHINERY INDUSTRY IN THE PRC

Cigarette production process and functions of our products

The following is a simplified diagram showing the principal production process of cigarettes, and the stages at which our main products as well as the other types of catalogued special-purpose tobacco machinery are applied during the production process of cigarettes. Further details regarding our products are set out in the paragraph headed “Products and services” in the section headed “Business” in this prospectus.



INDUSTRY OVERVIEW

Our Directors believe that our three types of catalogued special-purpose machinery products are crucial in the entire production process of cigarettes as:

- PP system is the machinery for compressing and packing of tobacco leaves, which have gone through the redrying process, into cartons with pre-determined size and volume for the convenience of transportation and storage in cigarette manufacturing factories. Without the application of such system, the tobacco leaves may need to be transported in loose form by trucks which could be subject to brokerage and loss during transit.
- Casing and flavouring system is designed to create the signature taste and texture of cigarettes by blending numerous kinds of flavours and casings according to the proprietary recipes and hence introduces the unique characteristics of each cigarette brand. By adding the various kinds of flavours and casings, our casing and flavouring system is also able to compensate for the loss in taste and texture caused by the reduction in tar contents in cigarettes required by the relevant government policies.
- PF system is a pneumatic-based machinery used to perform a task between two critical processes during the cigarette production processing, namely processing and packaging, by delivering the processed tobacco leaves through its enclosed pipe in a high speed manner to the cigarette wrapping machine. The application of PF system is regarded as a more cost-efficient approach since the application of feeding systems with traditional conveyer belts would give higher rates of brokerage and lower the production volume of cigarettes.

The end customers of our products and services are generally cigarette manufacturers and tobacco redrying factories in the PRC. According to China Tobacco Year Book 2009 published by STMA in December 2010, there were 30 cigarette industrial enterprises and 45 tobacco redrying factories in the PRC in 2009.

Competitive landscape of the catalogued special-purpose tobacco machinery industry

All manufacturers engaging in the sale and production of catalogued special-purpose tobacco machinery in the PRC have to obtain the Tobacco Production Licence. We believe the licensing regime itself creates a barrier of entry. There were 36 tobacco machinery manufacturers which have been granted the Tobacco Production Licence as at the end of 2008. Each of these licenced manufacturers was permitted to engage in the manufacture, sale and provision of maintenance, overhaul and modification services in one or more types of catalogued special-purpose tobacco machinery as listed on the Tobacco Machinery List. The number of tobacco machinery manufacturers which were permitted to engage in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of casing and flavouring systems, feeding systems and PP systems were 6, 18 and 3 respectively as at the end of 2008. PF system is a sub-class of feeding system listed on the Tobacco Machinery List. To the best of our Directors' knowledge, information and belief, there were about 3 domestic competitors engaged in the manufacture and sale of PF system as at the end of 2008. On the other hand, there were 17 tobacco machinery manufactures whose Tobacco Production Licence did not cover the manufacture and sale of casing and flavouring systems, feeding systems and PP systems.

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Based on the China Tobacco Year Book 2009 published in December 2010, the number of tobacco machinery manufacturers which have been granted the Tobacco Production Licence was reduced to 34 as at the end of 2009. As the two dropped out manufacturers which no longer possessed the Tobacco Production Licence were not permitted to engage in the manufacture and sale of casing and flavouring systems, PF systems and PP systems, to the best of our Directors' knowledge, information and belief, the number of domestic competitors engaged in the manufacture and sale of casing and flavouring systems, PF systems and PP systems remained at 6, 3 and 3 as at the Latest Practicable Date.

Based on publicly available information, the basic information of these competitors is set out as follows:

Company	Company background	Headquarters location	Competing products
Company A	A state-owned tobacco machinery manufacturer established in 1967 and reorganised in 2002.	Qinhuangdao, Hebei	Casing and flavouring systems, PP systems
Company B	A state-owned tobacco machinery manufacturer established in 1998.	Beijing	Casing and flavouring systems
Company C	A state-owned tobacco machinery manufacturer established in 1992.	Beijing	Casing and flavouring systems
Company D	A private tobacco machinery manufacturer established in 1996.	Changzhou, Jiangsu	Casing and flavouring systems, PF systems
Company E	A state-owned logistic machinery and tobacco machinery manufacturer established in 1970.	Kunming, Yunnan	Casing and flavouring systems, PP systems
Company F	A private tobacco machinery and mining machinery manufacturer established in 1966 and reorganised in 2008.	Zhangjiakou, Hebei	Casing and flavouring systems
Company G	A private logistic machinery and tobacco machinery manufacturer established in 1997.	Yangzhou, Jiangsu	PF systems
Company H	A private tobacco machinery manufacturer established in 1968.	Hangzhou, Zhejiang	PF systems
Company I	A state-owned tobacco machinery manufacturer established in 1981.	Kunming, Yunnan	PP systems

Competition in the current PRC catalogued special-purpose tobacco machinery industry is relatively moderate due to the limited number of participants. Nevertheless, for information about the challenges that we may face in this industry, please refer to the sub-section headed "Risks relating to the industry" in the section headed "Risk factors" in this prospectus.

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Procurement of catalogued special-purpose tobacco machinery

Pursuant to the Measures on Administration of Procurement, procurements of tobacco machinery listed on the Tobacco Machinery List must be approved by STMA. The Tobacco Machinery List sets out 22 types of catalogued special-purpose tobacco machinery deployed in the production of tobacco products and the Pricing Guidelines specifies the guidance price of different models of catalogued special-purpose tobacco machinery, whereas the Pricing Approval 2010 sets out the guidance price of various models of casing and flavouring systems not specified in the Pricing Guidelines. According to the Notice of STMA on Publication of the Tobacco Machinery List, the special-purpose tobacco machinery set out in the Tobacco Machinery List is defined as tobacco machinery which is able to complete one or more specific processes and is independently operated in the production and processing of tobacco raw materials and auxiliary materials. In order to meet the functional specification of the end customers, the catalogued special-purpose tobacco machinery may be customised and contain components and/or devices which are not listed in all of the Tobacco Machinery Documents but form integral parts of the customised systems. Having considered that these components and devices (i) are not standalone systems as defined in the Tobacco Machinery List; and (ii) are not listed in the Pricing Guidelines or Pricing Approval 2010, the PRC Legal Advisers are of the opinion that those components and devices should not be classified as catalogued special-purpose tobacco machinery and the requirements pursuant to the Measures on Administration of Procurement are not applicable to the sales of these items. Other types of tobacco machinery, which are not listed on the Tobacco Machinery List and which can be equipped with the catalogued special-purpose tobacco machinery in the production process of cigarettes, are referred to as non-catalogued ancillary tobacco machinery. Under the relevant regulations, domestic manufacturers engaging in the production of tobacco machinery as listed on the Tobacco Machinery List must possess the Tobacco Production Licence to engage in the manufacture and sale of the relevant tobacco machinery. According to the China Tobacco Year Book 2009 published by STMA in December 2010, as at the end of 2009, there were 34 tobacco machinery manufacturers which have been granted the Tobacco Production Licence for the manufacture and sale of various types of catalogued special-purpose tobacco machinery.

Pursuant to the Measures on Administration of Procurement, procurements of catalogued special-purpose tobacco machinery listed on the Tobacco Machinery List must be approved by STMA in advance. In addition, pursuant to these regulations, CTMC, being a subsidiary unit of CNTC, monitors and oversees all domestic made catalogued special-purpose tobacco machinery procurement matters between the tobacco machinery manufacturers and the cigarette manufacturers in the PRC. CTMC acts as a government agency to fulfill the relevant regulatory requirements in the procurement arrangements and is not involved in the negotiations regarding the transactions which are carried out between the tobacco machinery manufacturers and the purchasers. CTMC enters into sale and purchase agreements with the tobacco machinery manufacturers in connection with the machinery procurements made by cigarette manufacturers. The tobacco machinery manufacturers deliver the catalogued special-purpose tobacco machinery products directly to the cigarette manufacturers and tobacco redrying factories.

Pursuant to the 煙草行業機電產品進口管理辦法 (the Measures on Administration on Import of Mechanical and Electrical Products in the Tobacco Industry) promulgated by STMA in March 1994, a special division, namely 國家煙草專賣局機電產品進口辦公室 (the Mechanical and Electrical Products

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Import Office of STMA) was set up to administer the import of tobacco machinery. The Mechanical and Electrical Products Import Office of STMA makes a semi-annual plan for the imports of tobacco machinery with reference to the overall demand of technological transformation in the tobacco industry. Enterprises in the PRC planning to import tobacco machinery or relevant components and parts have to obtain prior approval from the Mechanical and Electrical Products Import Office of STMA and then procure the relevant products from the foreign tobacco machinery suppliers through China Tobacco Import and Export Company (中國煙草進出口總公司).

Background information on CTMC

Incorporated in 1988, CTMC plays a vital role in leading the long term development of the tobacco machinery industry in the PRC. CTMC is currently controlled as to 67% by CNTC. One of the main activities of CTMC is to formulate a system to manage the manufacture and sale of catalogued special-purpose tobacco machinery in China. According to the official website of STMA, the responsibilities of CTMC include, among others:

- participating in the formulation and organisation of the implementation of the development plan as well as the annual plan of the tobacco machinery industry in China;
- participating in the formulation of policies in respect of technological development of the tobacco machinery industry in China;
- promoting new technology and equipment;
- participating in the development of the pricing policies of domestic tobacco machinery;
- coordinating and monitoring tobacco machinery procurements in China; and
- coordinating domestic and foreign tobacco machinery technical cooperation, technical training as well as technical consulting services.

CTMC is also involved in the manufacture, sale, technology and quality development of catalogued special-purpose tobacco machinery and related products. CTMC controls the operations of four tobacco machinery manufacturers, namely, 秦皇島煙草機械有限責任公司 (Qinhuangdao Tobacco Machinery Co., Ltd.), 許昌煙草機械有限責任公司 (Xuchang Tobacco Machinery Co., Ltd.), 常德煙草機械有限責任公司 (Changde Tobacco Machinery Co., Ltd.) and 上海煙草機械有限責任公司 (Shanghai Tobacco Machinery Co., Ltd.), and three tobacco machinery technology development enterprises, namely, 北京達特煙草成套設備技術開發有限責任公司 (Beijing Date Complete Sets of Tobacco Equipment Technology Development Co., Ltd.), 北京特思達機電技術開發有限責任公司 (Beijing Tesida Mechanical and Electrical Technical Development Co., Ltd.) and 中煙機械技術中心有限責任公司 (China Tobacco Mechanical Technology Center Co., Ltd.). As the controlling shareholder of these enterprises, CTMC is entitled to exercise its rights of decision-making on major operating issues, controlling the arrangement of key managerial personnel and the administration of disciplinary inspection as well as supervision over their operations.

INDUSTRY OVERVIEW

Although CTMC plays a role in monitoring the catalogued special-purpose tobacco machinery industry in the PRC, our Directors believe that it is not one of CTMC's objectives to control the operations of all tobacco machinery manufacturers which possess the Tobacco Production Licence. To the best of our Directors' knowledge and information, some of the tobacco machinery manufacturers in China are privately owned enterprises. As advised by the PRC Legal Advisers, the current laws, rules and regulations in relation to catalogued special-purpose tobacco machinery industry in the PRC do not prohibit foreign-invested enterprises or private enterprises to engage in the manufacture of catalogued special-purpose tobacco machinery in the PRC, and the production of catalogued special-purpose tobacco machinery in compliance with the relevant Tobacco Production Licence by privately owned enterprises is protected by law.

Government policies in relation to the PRC tobacco industry

In order to meet the objectives set out in 煙草行業中長期科技發展規劃綱要(2006 – 2020年) (the Development Plan Outline for Medium and Long Term Technology Development in the Tobacco Industry (2006 – 2020)) issued by STMA in July 2006, STMA announced in 2006 that one of the core tasks in respect of technology innovation in the tobacco industry was the lowering of cigarette tar content. According to 國家煙草專賣局關於調整捲煙盒標焦油最高限量的通知 (the Notice of STMA Regarding the Adjustment of Maximum Tar Content Labeled on Cigarette Packages), effective from 1 January 2011, cigarettes with tar content exceeding 12 milligramme each will not be permitted for sale in the domestic market. The Directors believe that cigarette manufacturers will strive to formulate production technologies that could maintain the flavour of cigarettes despite the reduction of tar content. One of our main products, the casing and flavouring system, is designed to create the signature taste of individual cigarette brands according to the recipes of the cigarette manufacturers.

In view of the strategic plans proposed by STMA at the 2010 Annual National Tobacco Work Conference as described in the paragraph headed "Tobacco Industry in the PRC" in this section, our Directors consider that one of STMA's basic policies is to enhance the competitiveness and scale of domestic cigarette manufacturers, which in the opinion of our Directors, will drive consolidation amongst the industry participants. As a result, it is likely that cigarette manufacturers will grow larger in size and more resources will be spent on research and development in the tobacco industry. This, in turn, may create business opportunities for tobacco machinery manufacturers in the PRC.

REGULATORY OVERVIEW

OVERVIEW

Our operations are mainly carried out by our subsidiary, Baoying Renheng, in the PRC. The establishment and operations of Baoying Renheng shall comply with the following laws and regulations in respect of:

- incorporation, corporate governance, operation and management in compliance with, including but not limited to, 中華人民共和國公司法 (the Company Law of the PRC), 中華人民共和國外資企業法 (the Law of the PRC on Foreign-invested Enterprises), 外商投資產業指導目錄 (the Guiding Catalog of Foreign Investment Industries) and 指導外商投資方向規定 (the Provisions on Guiding the Direction of Foreign Investment);
- engaging in principal activities of manufacturing of catalogued special-purpose tobacco machinery in accordance with, including but not limited to, the Law of PRC on Tobacco Monopoly, the Rules for Implementation of the Law of the PRC on Tobacco Monopoly, 煙草專賣許可證管理辦法 (the Measures on Administration of Tobacco Monopoly Licence), 煙草專用機械專賣管理辦法(試行) (the (Trial) Measures on Administration of Sales of Catalogued Special-purpose Tobacco Machinery Monopoly) and other related laws and regulations;
- product quality management in compliance with 中華人民共和國民法通則 (the General Principles of the Civil Laws of the PRC), 中華人民共和國產品質量法 (the Product Quality Law of the PRC), 中華人民共和國消費者權益保護法 (the Law of the PRC on the Protection of the Rights and Interests of Consumers), 煙草行業產品質量監督檢驗網管理辦法 (the Administrative Measures on Supervision and Inspection of Product Quality in Tobacco Industry) and other related laws and regulations;
- foreign exchange, shareholder loans, dividend distribution, outward remittance and overseas investment under current accounts and capital accounts in accordance with 中華人民共和國外匯管理條例 (the Foreign Exchange Administration Regulations of the PRC), 結匯、售匯及付匯管理規定 (the Regulations on the Administration of Foreign Exchange Settlement, Sale and Payment) and other related laws and regulations;
- tax payment and filing of tax returns in accordance with 中華人民共和國企業所得稅法 (the Enterprise Income Tax Law of the PRC), 內地和香港特別行政區關於對所得避免雙重徵稅和防止偷漏稅的安排 (the Arrangement between Mainland China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and Prevention of Fiscal Evasion with respect to Taxes on Income), 中華人民共和國增值稅暫行條例 (the PRC Provisional Regulations on Value-added Tax) and other related laws and regulations;
- environmental protection measures in compliance with 中華人民共和國環境保護法 (the Environment Protection Law of PRC), 中華人民共和國水污染防治法 (the Water Pollution Prevention and Control Law of PRC) and other related laws and regulations;

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- employment and social security liabilities in compliance with 中華人民共和國勞動法 (the PRC Labour Law), 中華人民共和國勞動合同法 (the PRC Labour Contract Law), 社會保險登記管理暫行辦法 (the Interim Provisions on Registration of Social Insurance), 社會保險費徵繳暫行條例 (the Interim Regulation on the Collection and Payment of Social Insurance Premiums) and other related laws and regulations;
- manufacturing safety management in compliance with 中華人民共和國安全生產法 (the PRC Production Safety Law) and other related laws and regulations;
- intellectual property management and protection in accordance with 中華人民共和國專利法 (the PRC Patent Law) and other related laws and regulations.

The following sections describe the laws, rules and regulations to which we are subject that we believe are important for a potential investor to understand.

LAWS, RULES AND REGULATIONS IN RELATION TO CATALOGUED SPECIAL-PURPOSE TOBACCO MACHINERY INDUSTRY IN THE PRC

The catalogued special-purpose tobacco machinery industry in the PRC is strictly overseen and supervised by government authorities. STMA is responsible for administration of the national tobacco monopoly and also the policy making and the promulgation of all laws, rules and regulations for the production and sales of catalogued special-purpose tobacco machinery. National Development and Reform Commission is responsible for the promulgation of regulations in relation to the application, approval and supervision of tobacco monopoly licence.

Baoying Renheng, as one of the catalogued special-purpose tobacco machinery manufacturers in the PRC, is overseen and supervised by STMA and local tobacco monopoly authorities and is subject to the laws, rules and regulations promulgated by National Development and Reform Commission and STMA. The major PRC laws, rules and regulations applicable to Baoying Renheng include the Law of the PRC on Tobacco Monopoly, the Rules for Implementation of the Law of the PRC on Tobacco Monopoly, the Measures on Administration of Tobacco Monopoly Licence, the (Trial) Measures on Administration of Sales of Catalogued Special-purpose Tobacco Machinery Monopoly, the Measures on Administration of Procurement, 煙草專用機械產品購銷合同管理辦法 (the Measures on Administration of Sale and Purchase Contracts of Catalogued Special-purpose Tobacco Machinery), 煙草機械產品售後服務管理辦法 (the Measures on Administration of After-sales Services for Tobacco Machinery) and 煙草專用機械設備大修管理辦法 (the Measures on Administration of Major Repair of Catalogued Special-purpose Tobacco Machinery).

A summary of the major law, rules and regulations and the respective implementation methods in respect of catalogued special-purpose tobacco machinery industry in the PRC is set out below.

REGULATORY OVERVIEW

Tobacco machinery list

On 12 August 1992, STMA promulgated 國家煙草專賣局關於公佈煙草專用機械名錄的通知 (the Notice of STMA on Publication of the Tobacco Machinery List) (GUO YAN FA [1992] No.18), and 28 types of catalogued special-purpose tobacco machinery were included in the list. On 1 June 2004, STMA published and implemented the revised Tobacco Machinery List, and 22 types of catalogued special-purpose tobacco machinery have been included in the Tobacco Machinery List. Casing and flavouring system, PF system and PP systems are all catalogued special-purpose tobacco machinery specified in the Tobacco Machinery List.

Tobacco production licence

Manufacture of tobacco products in the PRC is subject to certain licensing requirements. Pursuant to the Law of PRC on Tobacco Monopoly and its implementation regulations, enterprises engaging in the manufacture and sale of catalogued special-purpose tobacco machinery as listed on the Tobacco Machinery List must file an application to the department of tobacco monopoly administration under the State Council to obtain the Tobacco Production Licence before the enterprises are permitted to manufacture catalogued special-purpose tobacco machinery as listed on the Tobacco Machinery List. As our casing and flavouring systems, PF systems and PP systems are catalogued special-purpose tobacco machinery specified in the Tobacco Machinery List, we are required to obtain the Tobacco Production Licence in order to carry out catalogued special-purpose tobacco machinery manufacturing. We have obtained the Tobacco Production Licence which is valid for a period of five years commencing on 14 April 2009 and expiring on 14 April 2014.

Pursuant to the Measures on Administration of Tobacco Monopoly Licence promulgated by STMA on 11 May 1998, which is further revised by National Development and Reform Commission and promulgated on 5 February 2007, the maximum validity of the Tobacco Production Licence is five years and shall be calculated from the date of issuing the licence. In case that the enterprise needs to continue the production and/or operation after the expiry of the licence, such enterprise shall submit an application to the original licensing authority for renewal thirty days before its expiry. As such, our Tobacco Production Licence is subject to renewal by STMA upon its expiry.

Sales of catalogued special-purpose tobacco machinery

Pursuant to the Law of the PRC on Tobacco Monopoly and its implementation regulations, catalogued special-purpose tobacco machinery manufacturers can only sell their catalogued special-purpose tobacco machinery to tobacco companies and tobacco product manufacturers which possess the Tobacco Production Licence. In addition, the Rules for Implementation of the Law of the PRC on Tobacco Monopoly provide that wholesalers of tobacco monopoly commodities and tobacco products manufacturing enterprises can purchase catalogued special-purpose tobacco machinery only from enterprises with 特種煙草專賣經營企業許可證 (Special Tobacco Monopoly Operating Enterprise Licence). The enterprise with special tobacco monopoly operating enterprise licence is allowed to engage in import and export business of tobacco monopoly commodities. According to the Law of the PRC on Tobacco Monopoly, tobacco monopoly commodities refer to cigarettes, cigars, cut tobacco, redried leaf tobacco, leaf tobacco, cigarette paper, filter rods, cigarette tow and catalogued special-purpose tobacco machinery.

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1. Purchase order of catalogued special-purpose tobacco machinery

Pursuant to the Measures on Administration of Procurement promulgated and implemented on 1 January 2004, enterprises purchasing catalogued special-purpose tobacco machinery shall send the purchase report to the direct reporting unit or competent state administrative bureau or authority (hereinafter collectively referred to as “Provincial Tobacco Monopoly Authority”) for approval. If the Provincial Tobacco Monopoly Authority has no objection on the purchase report, they shall send the report to STMA attached with their opinions. Competent authority under STMA which is in charge of fixed assets investment shall issue a purchase approval document on purchasing tobacco machinery regulated by STMA.

2. Purchase contract of catalogued special-purpose tobacco machinery

Pursuant to the Measures on Administration of Sale and Purchase Contracts of Catalogued Special-purpose Tobacco Machinery promulgated on 9 September 1996, CNTC designates CTMC to deal with the sale and purchase contracts in relation to tobacco machinery. CTMC, as the buyer, places order with the designated tobacco machinery manufacturers to buy tobacco machinery, or as the vendor to sell tobacco machinery to tobacco industrial enterprises (including cigarette factories, cigar factories, tobacco redrying factories, cigarette material factories). The sale and purchase contracts of catalogued special-purpose tobacco machinery shall be concluded in written form with the buyer and the vendor. The contract can be executed only after the buyer has shown the purchase approval document. The main terms of the contract shall include the name of the tobacco machinery, item number, specification, quantity, quality requirement, price, delivery method, time and place of delivery, transportation mode, acceptance method, payment settlement, responsibility of default and other items agreed by the two parties.

Repair of catalogued special-purpose tobacco machinery

According to the Measures on Administration of Major Repair of Catalogued Special-purpose Tobacco Machinery promulgated and implemented on 13 September 2000, tobacco machinery manufacturers with Tobacco Production Licence issued by STMA shall be the designated enterprises for the repair of tobacco machinery made by the enterprises with licence.

Transportation of tobacco monopoly commodities

Pursuant to the Rules for Implementation of the Law of the PRC on Tobacco Monopoly, when transporting the domestic made catalogued special-purpose tobacco machinery across different provinces, autonomous regions and municipalities, a delivery permit of tobacco monopoly commodities must be obtained from the department of tobacco monopoly administration under the State Council or its authorised agencies. When transporting the domestic made catalogued special-purpose tobacco machinery across different cities and towns within a province, an autonomous region or a municipality, a delivery permit of tobacco monopoly commodities must be obtained from the department of tobacco monopoly administration of provincial level or its authorised agencies. The administrative measures for the delivery permit of tobacco monopoly commodities shall be stipulated by the department of tobacco monopoly administration under the State Council.

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According to 煙草專賣品准運證管理辦法 (the Measures on Administration of the Delivery Permit of Tobacco Monopoly Commodities) promulgated and implemented on 4 June 2002, a delivery permit of tobacco monopoly commodities is required for transporting catalogued special-purpose tobacco machinery. Tobacco monopoly administration of provincial level (or above) is responsible for the issuing of the delivery permit. The valid period of the delivery permit shall be determined by the issuing authority of tobacco monopoly according to the distance and mode of the transportation applied by the applicant. The validity of delivery permit of tobacco monopoly commodities shall not exceed twenty days by way of highway transportation and not more than thirty days by way of other means of transportation. The validity of delivery permit of tobacco monopoly commodities shall be calculated from the date of issue.

Continuous supervision of tobacco monopoly administration

According to the Rules for Implementation of the Law of the PRC on Tobacco Monopoly, the issuing authority of the Tobacco Production Licence has the right to inspect the enterprises and/or individuals with Tobacco Production Licence. For enterprises and/or individuals with Tobacco Production Licence who do not meet the requirements of the Law of PRC on Tobacco Monopoly and the above-mentioned rules, they will be subject to penalty, fine and/or confiscation of the proceeds from the activity which is deemed non-compliant with the relevant laws, rules or regulations. The licensing authority of tobacco monopoly also has the right to order the suspension and rectification of tobacco monopoly business or even cancel the qualification of the enterprise to deal with tobacco monopoly business. According to the Rules for Implementation of the Law of the PRC on Tobacco Monopoly, delivery of tobacco monopoly commodities without delivery permit or in excess of the approved quantities is subject to the possible penalty of a fine equivalent to 20% to 50% of the value of the relevant tobacco monopoly commodities. Furthermore, production of cigarette paper, filter rods, cigarette tow and catalogued special-purpose tobacco machinery without the Tobacco Production Licence is subject to the possible penalty of a fine equivalent to 1 to 2 times of the value of the relevant tobacco monopoly commodities.

國家煙草專賣局關於進一步加強煙機專賣管理的通知 (The Notice of STMA Regarding the Further Strengthening of Tobacco Monopoly Administration) provides that the designated enterprises of manufacturing tobacco machinery must strictly comply with the provisions of the Law of the PRC on Tobacco Monopoly and the tobacco machinery monopoly administration, and report the relevant information with respect to the production and sales of tobacco machinery to the local and provincial tobacco monopoly administration where the enterprise is located. All the provincial tobacco monopoly administration shall make annual inspection of the designated tobacco machinery manufacturing enterprises under the leadership of STMA and all the tobacco machinery manufacturing enterprises must recognise and actively cooperate with the supervision and inspection of the department of tobacco monopoly administration.

The Measures on Administration of Catalogued Special-purpose Tobacco Machinery Monopoly also clearly provides that the tobacco machinery manufacturing enterprises must accept the inspection and supervision of department of tobacco monopoly administration under STMA. Furthermore, the tobacco machinery production enterprises shall report to the provincial supervision administration of tobacco monopoly semi-annually about the production and sales information of their products.

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REGULATIONS IN RELATION TO TOBACCO CONTROL

Pursuant to 公共場所衛生管理條例實施細則 (Implementation Rules on the Administrative Regulation of Public Place Sanitation) which was promulgated on 11 March 1991 and implemented on 1 June 1991 by 中華人民共和國衛生部 (Ministry of Health of the PRC), smoking in 14 public indoor places including, among others, theatres, ballrooms, game rooms, gymnasiums, libraries, museums and shops is prohibited. The new Implementation Rules on the Administrative Regulation of Public Place Sanitation which was promulgated on 10 March 2011 and implemented on 1 May 2011 provides that smoking in 28 public indoor places including, among others, hotels, restaurants, bars, theatres, game rooms, parks, exhibition halls, waiting rooms and public transports as set out in 公共場所衛生管理條例 (Administrative Regulation of Public Place Sanitation) is prohibited. Business operators in public places should carry out promotions on health hazards caused by smoking and delegate personnel or part-time staff to discourage smokers from smoking. In addition, pursuant to 民用機場和民用航空器內禁止吸煙的規定 (Regulation on Smoking Ban in Civil Airports and Civil Aviation Carriers) promulgated and implemented on 30 December 1997 and 互聯網上網服務營業場所管理條例 (Administrative Regulation of Internet Access Service Business Premises) implemented on 15 November 2002, smoking in certain areas of civil airports and the whole civil aircrafts as well as business premises providing internet access services is also prohibited.

COMPANY LAW OF THE PRC

The establishment and operation of our sole operating subsidiaries in the PRC, Baoying Renheng, is governed by the Company Law of the PRC, which was promulgated by the Standing Committee on 29 December 1993 and became effective on 1 July 1994. It was subsequently amended on 25 December 1999, 28 August 2004, and 27 October 2005.

The Company Law of the PRC recognises two general types of companies, namely limited liabilities companies and joint stock limited companies. Both types of companies have the status of legal person, and the liability of a company to its debtors is limited to the value of assets owned by the company. Liability of shareholders of a limited liability company and a joint stock limited company is limited to the amount of registered capital and shares they have contributed.

The amendments to the Company Law of the PRC adopted in October 2005 seek to make reform in the establishment and operation procedures of companies and provide that the Company Law of the PRC shall apply to foreign invested limited liability companies and foreign-invested joint stock companies subject to stipulations otherwise provided by the laws on foreign investment.

LAW RULES AND REGULATIONS IN RELATION TO QUALITY MANAGEMENT

According to the Measures on Administration of Sale and Purchase Contracts of Catalogued Special-purpose Tobacco Machinery, the quality of tobacco machinery must comply with the industry standards, where there is no such industrial standards, the enterprise's standard. The Administrative Measures on Supervision and Inspection of Product Quality in Tobacco Industry promulgated and implemented on 28 September 2001 provide that the quality inspection and supervision duties for tobacco industry shall be administrated by the competent authority for quality and technical supervision

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under STMA (hereinafter referred to as “competent authority under STMA”) and its basic task is to undertake regular quality supervision and inspection for tobacco monopoly products and the related products (hereinafter referred to as “tobacco products”) as well as inspections when there is arbitration. The network of quality inspection for tobacco industry consists of three-levels:

- (i) National Quality Inspection Agency (first-class agency) is the highest authority in respect of quality inspection in the tobacco industry as approved by 中華人民共和國國家質量監督檢驗檢疫總局 (the General Administration of Quality Supervision, Inspection and Quarantine of the PRC, originally named as 國家質量技術監督局 (State Bureau of Quality and Technical Supervision)). This agency shall be under the supervision of STMA and its authorised affiliated unit and its operation shall be subject to the guidance of the General Administration of Quality Supervision, Inspection and Quarantine of the PRC;
- (ii) Provincial (or regional) Quality Inspection Agency (second-class agency), approved and authorised by STMA, is the authority for the quality inspection and supervision of tobacco quality at provincial or regional level. It is subject to the supervision of STMA and competent provincial tobacco monopoly administration or its affiliated unit and its operation shall be subject to the guidance of the National Quality Inspection Agency and provincial-level Quality and Technical Supervision Bureau where it is located; and
- (iii) Enterprise-level Quality Inspection Agency (third-class agency) is the product quality checkpoint within the cigarette factory, tobacco-affiliated enterprises and tobacco companies located in the major production area and major tobacco market. It is responsible for quality inspection and supervision of tobacco companies and products within such area. This agency shall be subject to the supervision of competent provincial tobacco monopoly administration and the relevant subordinating unit, and its operation shall be subject to the guidance of the provincial-level Quality Inspection Agency and the local Quality and Technical Supervision Bureau.

LAWS, RULES AND REGULATIONS IN RELATION TO FOREIGN INVESTMENTS IN THE PRC

The establishment, operation and management of Baoying Renheng shall be governed by 中華人民共和國中外合資經營企業法 (the Law of the PRC on Chinese-foreign Equity Joint Ventures), the Law of the PRC on Foreign-invested Enterprises, and their implementation rules. The Law of the PRC on Chinese-foreign Equity Joint Ventures was promulgated on 1 July 1979 and amended twice on 4 April 1990 and 15 March 2001 respectively, and the Law of the PRC on Foreign-invested Enterprises was promulgated on 12 April 1986 and amended on 31 October 2000.

In accordance with the Guiding Catalog of Foreign Investment Industries jointly promulgated by the National Development and Reform Commission and the Ministry of Commerce on 31 October 2007, the catalogued special-purpose tobacco machinery manufacturing business of Baoying Renheng does not fall within the range of the encouraged, restricted or prohibited foreign investment industries as described above. In addition, according to the relevant stipulations in the Provisions on Guiding the Direction of Foreign Investment, any foreign investment projects not falling within the range of

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the encouraged, restricted or prohibited foreign investment industries shall fall into the category of permitted projects. The manufacturing business of catalogued special-purpose tobacco machinery carried out by Baoying Renheng, a wholly foreign-owned subsidiary of our Company, falls within the range of permitted foreign investment industries.

LAWS AND REGULATIONS IN RELATION TO FOREIGN EXCHANGE

China mainly has two foreign exchange administrative regulations, namely the Foreign Exchange Administration Regulations of the PRC, which were promulgated by the State Council on 29 January 1996, and amended on 14 January 1997 and 1 August 2008, and the Regulations on the Administration of Foreign Exchange Settlement, Sale and Payment, which were promulgated by the PBOC on 20 June 1996. According to the abovementioned foreign exchange administrative regulations, upon payment of the applicable taxes, FIEs may convert the dividends they receive in Renminbi into foreign currencies and remit such amounts outside the PRC through their foreign exchange bank accounts. Generally, FIEs may engage in foreign exchange transactions by converting Renminbi into foreign currencies and remitting the relevant amounts out of the PRC without the prior approval of SAFE under two situations: (i) when an enterprise needs to settle current account items in foreign currencies; and (ii) when an enterprise needs to distribute dividends to its foreign shareholders.

In other situations, including the settlement of capital account items, FIEs are subject to the above administrative regulatory restrictions on foreign exchange. They must seek prior approval from SAFE or its relevant branches before converting Renminbi into foreign currencies.

Dividend distribution and remittance

In accordance with the Law of the PRC on Foreign-invested Enterprises promulgated on 12 February 1986 and amended on 31 October 2000, foreign investors may remit dividends distributed by a wholly foreign-owned enterprise overseas. Under the Rules for the Implementation of the Law of the PRC on Foreign-invested Enterprises promulgated on 12 December 1990 and amended on 12 April 2001, a wholly foreign owned enterprise, may distribute dividends out of its profits after it has set aside at least 10% of after-tax profit for its reserve fund (no after-tax profit needs to be set aside once the cumulative amount of the reserve fund reaches 50% of the registered capital of the WFOE) and, at its discretion, has allocated a portion of its after-tax profits to the staff welfare and bonus fund.

LAWS AND REGULATIONS IN RELATION TO SHAREHOLDER LOANS

In accordance with the 外匯管理條例 (Regulations on Exchange Control) and 外債管理暫行辦法 (the Administration of Foreign Debts Tentative Procedures), China implements a scale management on foreign debts. Shareholder loans of FIEs shall be viewed as foreign debts borrowing and shall be handled in accordance with the relevant regulations of the PRC and are required to apply to relevant foreign exchange authorities for registration of foreign debts. The sum of accumulative amount of mid/long-term foreign debts and the balance of short-term foreign debts of FIEs shall be controlled within the limits of difference between the total investment approved by approving authority and the registered capital. The FIEs may borrow foreign loans at its own discretion, which shall be within the difference amount. For those beyond the difference limits, the company shall apply to the former approving authority for the re-approval of the total investment for the project.

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LAWS, RULES AND REGULATIONS IN RELATION TO TAXATION

Enterprise income tax

On 1 January 2008, 中華人民共和國外商投資企業和外國企業所得稅法 (the Foreign-invested Enterprise and Foreign Enterprise Income Tax Law of the PRC) was abolished, and the Enterprise Income Tax Law of the PRC, promulgated on 16 March 2007, became effective. Pursuant to the Enterprise Income Tax Law of the PRC, the income tax rate for both domestic-funded enterprises and foreign-invested enterprises is 25%.

Pursuant to the Notice on the Implementation of the Enterprise Income Tax Transition Preferential Policy (國務院關於實施企業所得稅過度優惠政策的通知), enacted by the State Council of the PRC on 26 December 2007, enterprises that had enjoyed the preferential policy of a full exemption in the first two years and a 50% reduction from the third to the fifth years of the income tax since the first profit-making year, shall continue to enjoy the former policy after the implementation of the New Enterprise Income Tax Law until the preferential period expired; enterprises that were entitled to but had not enjoyed the aforesaid preferential policy due to their failure to make profit shall enjoy the aforesaid preferential policy from 2008.

Furthermore, unlike the Foreign-invested Enterprise and Foreign Enterprise Income Tax Law of the PRC, which specifically exempted withholding income tax on any dividends payable to non-PRC enterprise investors, the Enterprise Income Tax Law of the PRC provides that an income tax rate of 20% will normally be applicable to dividends payable to non-PRC enterprise investors which are derived from sources within the PRC, unless there exists a preferential tax treatment between the PRC and the relevant jurisdictions in which such non-PRC enterprise shareholders reside whereupon the relevant tax may be reduced or exempted. However, pursuant to the Implementation Rules of the Enterprise Income Tax Law of the PRC promulgated by the State Council on 6 December 2007 and effective on 1 January 2008, a reduced income tax rate of 10% will be applicable to any dividends payable to non-PRC enterprise investors from foreign-invested enterprises.

Moreover, according to the Arrangement between Mainland China and the Hong Kong Special Administrative Region for the Avoidance of Double Taxation and Prevention of Fiscal Evasion with respect to Taxes on Income, the PRC tax resident enterprise which distributes dividends to its Hong Kong shareholders should be levied enterprise income tax according to PRC law. However, if the beneficiary of the dividends is a Hong Kong tax resident, which directly holds not less than 25% equity of the aforesaid enterprise (i.e. the dividends distributor), the tax levied should be 5% of the distributed dividends. If the beneficiary of the dividends is a Hong Kong tax resident, which directly holds less than 25% equity of the aforesaid enterprise, the tax levied should be 10% of the distributed dividends.

Value-added tax

Pursuant to the PRC Provisional Regulations on Value-added Tax, which was promulgated by the State Council on 13 December 1993 and amended on 10 November 2008, and their implementation rules, any enterprise or individual engaged in the sale of goods, the provision of specified services or

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the importation of goods in the PRC is generally required to pay value-added tax on the added value derived during the process of manufacture, sale or the provision of services. Unless stated otherwise, value-added tax payers who are engaged in sales or import of goods, provision of processing, repair and replacement services in the PRC are subject to a tax rate of 17%.

LAWS, RULES AND REGULATIONS IN RELATION TO ENVIRONMENTAL PROTECTION

The PRC Government has formulated and implemented various environmental protection laws and regulations, including 中華人民共和國環境保護法 (the Environment Protection Law of PRC), 中華人民共和國水污染防治法 (the Water Pollution Prevention and Control Law of PRC), 中華人民共和國大氣污染防治法 (the Atmospheric Pollution Prevention and Control Law of PRC), 中華人民共和國固體廢物污染環境防治法 (the Solid Waste Environment Protection and Control Law of PRC), 中華人民共和國環境噪聲污染防治法 (the Environmental Noise Pollution Prevention and Control Law of PRC) and 中華人民共和國環境影響評價法 (the Environmental Impact Evaluation Law of PRC). Under the relevant environmental protection laws and regulations, the construction, expansion and operation of production facilities are subject to certain government evaluation process, inspection procedures and approvals. Failure to go through such government process or procedures or to obtain such government approvals may subject the manufacturer to fines and penalties imposed by the relevant PRC environmental authorities, including suspension of the production facilities.

The relevant environmental protection laws also impose fees for the discharge of waste substances, permit the imposition of fines and compensation for the improper discharge of waste substances and serious environmental offences. The PRC environmental authorities may, at their discretion, close any facility that fails to comply with orders requiring it to rectify or cease operations causing the environmental damage.

LAWS, RULES AND REGULATIONS IN RELATION TO LABOUR LAW AND WELFARE SCHEMES

Enterprises are mainly subject to the following PRC labour laws and regulations: the PRC Labour Law, the PRC Labour Contract Law, 中華人民共和國社會保險法 (Social Insurance Law of the People's Republic of China), 工傷保險條例 (the Regulation of Insurance for Work-Related Injury), 失業保險條例 (the Regulations on Unemployment Insurance), 企業職工生育保險試行辦法 (the Provisional Measures on Insurance for Maternity of Employees), the Interim Provisions on Registration of Social Insurance, the Interim Regulation on the Collection and Payment of Social Insurance Premiums, and other related regulations, rules and provisions issued by the relevant governmental authorities from time to time for enterprises in the PRC.

Pursuant to the PRC Labour Law and the PRC Labour Contract Law, labour contracts in written form shall be executed to establish labour relationships between employers and employees. Salaries shall not be lower than local minimum wage. The company must establish a system for labour safety and sanitation, strictly abide by state standards, and provide relevant education to its employees. Employees are also required to work in safe and sanitary conditions meeting State rules and standards, and carry out regular health examinations for employees engaged in hazardous occupations.

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As required under the Social Insurance Law of the People's Republic of China, the Regulation of Insurance for Work-Related Injury, the Regulations on Unemployment Insurance, the Provisional Measures on Insurance for Maternity of Employees, the Interim Provisions on Registration of Social Insurance and the Interim Regulation on the Collection and Payment of Social Insurance Premiums, the subsidiary of our Company in the PRC is obliged to provide employees in the PRC with welfare schemes covering pension insurance, unemployment insurance, maternity insurance, injury insurance and medical insurance.

In accordance with 住房公積金管理條例 (the Regulations on Management of Housing Provident Fund) promulgated on 3 April 1999 and amended on 24 March 2002, Baoying Renheng must apply to relevant Housing Provident Fund Management Center for the registration of payment and deposit, and open housing fund account with a specified bank for employees' fund payment and deposit. In addition, the percentage of housing provident fund for each employee shall be no less than 5% of his/her average monthly salary in last year.

LAWS, RULES AND REGULATIONS IN RELATION TO PRODUCTION SAFETY

Pursuant to the PRC Production Safety Law which became effective on 1 November 2002 and was amended on 27 August 2009, 國家安全生產監督管理總局 (the State Administration of Work Safety) is in charge of the overall administration of production safety. The Safety Production Law provides that an entity engaging in manufacturing activities must meet national or industry standards regarding safety production and provide relevant working conditions as required by the laws, administrative rules and the national or industry standards. An entity engaging in manufacturing activities must install prominent warning signs at or on relevant dangerous operation sites, facilities and equipment. The design, production, installment, use, test, repair, upgrade and disposal of safety equipment must comply with national or industry standards.

As a catalogued special-purpose tobacco machinery manufacturer, Baoying Renheng shall comply with relevant stipulations in the PRC Production Safety Law, provide safe production conditions according to the law, and shall provide education and training on work safety to employees.

LAWS, RULES AND REGULATIONS IN RELATION TO PRODUCT LIABILITY

Manufacturers and vendors of defective products in the PRC may incur liability for loss and injury caused by such products. Under the General Principles of the Civil Laws of the PRC, which became effective on 1 January 1987, a defective product which causes property damage or physical injury to any person could subject the manufacturer or retailer of such product to civil liability for such damage or injury.

The General Principles of the Civil Laws of the PRC were supplemented by the Product Quality Law of the PRC which was promulgated on On 22 February 1993, amended on 8 July 2000 and 27 August 2009, and the Law of the PRC on the Protection of the Rights and Interests of Consumers which was promulgated on 31 October 1993, amended on 27 August 2009, were enacted to protect the legitimate rights and interests of end-users and consumers and to strengthen the supervision and control of the quality of products. If products purchased by consumers are of sub-standard quality but not defective, the retailers will be responsible for the repair, exchange, or refund of the purchase

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price of the sub-standard products and for the compensation to the consumers for their losses (if any). However, in the event that the manufacturers are liable for the sub-standard products, the retailers are entitled to seek reimbursement from the manufacturers for compensation paid by the retailers to the consumers. If the products are defective and cause any personal injuries or damage to assets, the consumer has the option to claim compensation from the manufacturer, distributor or retailer. Retailers or distributors who have already compensated the consumers are entitled to claim reimbursement from the liable manufacturers.

LAWS, RULES AND REGULATIONS IN RELATION TO PATENTS

According to the PRC Patent Law which was promulgated on 12 March 1984, amended on 25 August 2000 and 27 December 2008 respectively, patent protection is divided into three categories: invention patents, utility patents and design patents. Invention patents are intended to protect new technical solutions for a product, method or its improvement. Utility patents are intended to protect new technical solutions for a product's shape, structure or the combination of both shape and structure, which are applicable for the utility. Design patents are intended to protect new designs of the shape, pattern or the combination of both shape and pattern, or the combination of the color with shape or pattern of a product with aesthetic and industrial application value.

Invention patents

Products seeking invention patent protection must possess novel and innovative characteristics, and the grant of an invention patent is subject to disclosure and publication. In the PRC, 中華人民共和國國家知識產權局 (the State Intellectual Property Office of the PRC) publishes the application within 18 months after it is filed, which period may be shortened upon request by the applicant. After the application is published, the State Intellectual Property Office conducts a substantive review upon request by the applicant within three years from the filing date of the application at its discretion to grant the invention patent, issue the certificate of invention patent, announce and register the patent if there is no cause for rejection of the application of the invention patent after substantive review and make a decision. The protection period for an invention patent is 20 years from the date of application.

Once an invention patent is granted, unless otherwise permitted by law, no individuals or entities are permitted to engage in the manufacture, use, sale or import of the products protected by such patent or otherwise engage in the manufacture, use, sale or import of the products directly derived from applying the production skills or methods protected by such patent, without consent of the patent holder.

Utility patents

Products seeking utility patent protection must also possess novel and innovative characteristics. Utility patents are granted and registered upon application unless there are reasons for the State Intellectual Property Office to reject the application after preliminary review. Utility patents are also subject to disclosure and publication upon application. The protection period for a utility patent is ten years from the date of application.

REGULATORY OVERVIEW

Once a utility patent is granted, unless otherwise permitted by law, no individuals or entities are permitted to engage in the manufacture, use, sale or import of the products protected by such patent without consent of the patent holder.

Design patents

The products seeking design patent protection must not be the same as or similar to those previously known in domestic or abroad or infringing upon third parties' legal rights. The application procedures and protection period are the same as utility patents.

Once a design patent is granted, no individuals or entities are permitted to engage in the manufacture, use, sale or import of the products protected by such patent without consent of the patent holder.

REGULATIONS IN RELATION TO REGISTERED TRADEMARKS

Pursuant to 中華人民共和國商標法 (Trademark Law of the PRC) promulgated in 1982 and amended in 2001, the right to exclusive use of a registered trademark is limited to the trademark which has been approved for registration and the commodities under the relevant class specification of the registered trademark. Furthermore, under the Trademark Law of the PRC, any of the following acts shall be regarded as an infringement upon the right to exclusive use of a registered trademark, including (i) using a trademark which is identical with or similar to the registered trademark on the same or similar commodities without obtaining authorisation from the trademark registrant; (ii) selling the commodities that infringe upon the right to exclusive use of a registered trademark; (iii) forging, manufacturing the marks of a registered trademark of others without authorisation, or selling the marks of a registered trademark forged or manufactured without authorisation; (iv) altering a registered trademark and launching commodities with the altered trademark in the market without authorisation; and (v) causing other damage to the right to exclusive use of a registered trademark of another person. Pursuant to 中華人民共和國商標法實施條例 (Regulation on Implementation of Trademark Law of the PRC) promulgated in 2002, where a holder of a registered trademark which has been recognised as a well known trademark considers that the registration of the relevant trademark as an enterprise name by any other person is likely to deceive, or mislead, the public, the trademark holder may file an application with the competent authority for the registration of the enterprise name to revoke such registration.

REGULATORY COMPLIANCE

Our Directors, as advised by our legal advisers, confirmed that we had complied with all applicable laws and regulations in all material respects during the Track Record Period. We have obtained approvals, licences and permits necessary for our operations in the jurisdictions where we operated throughout the Track Record Period.

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To ensure on-going compliance with relevant regulatory requirements, we have set up a compliance committee in June 2011, headed by Mr. Sun Zhaohui, the chief executive officer of our Company. Members of the compliance committee comprise all the department heads of Baoying Renheng and the company secretary of our Company. Mr. Sun, as the chairman of the compliance committee, has defined clear responsibilities for each committee member to ensure compliance with relevant regulatory requirements. We have compiled a list setting out the requirements under applicable laws, rules and regulations and a register containing details of all approvals, licences and permits necessary for our operations. Such list and register have been reviewed by the PRC Legal Advisers and approved by Mr. Sun. The compliance committee will meet quarterly to keep the members abreast of the latest regulatory requirements and to report irregularities as well as remedial measures taken (where applicable). Our independent non-executive Directors will review the operations of the compliance committee on a semi-annual basis and report to the Board on any deficiency identified as well as the recommendation for appropriate rectifying action (where applicable).

HISTORY AND DEVELOPMENT

CORPORATE DEVELOPMENT

The history of our Group can be traced back to August 2001 when Baoying Radio Factory (寶應縣無線電廠), a then state-owned enterprise which was principally engaged in the manufacture of tobacco machinery and automation control systems, underwent an ownership reform program under which Baoying Machinery and Electronics Company Limited (寶應縣機械電子工業公司) was authorised by the People's Government of Baoying (寶應縣人民政府) to enter into a sale and purchase agreement dated 30 August 2001 with Yanlord Industrial in relation to the acquisition of certain assets of Baoying Radio Factory by Yanlord Industrial. Yanlord Industrial was incorporated in Hong Kong on 21 July 1992 and owned as to 5% by Mr. Wei and 95% by Mr. Zhong Sheng Jian, Mr. Wei's uncle, both being the founders of our Group. Pursuant to the said sale and purchase agreement, Yanlord Industrial agreed to acquire 80% of the net assets of Baoying Radio Factory (excluding certain receivables, investments, property interests and liabilities) ("Adjusted Net Assets") at a cash consideration of RMB14.4 million and undertook to employ 275 former employees of Baoying Radio Factory. The consideration was arrived at after arm's length negotiation between the parties thereto with reference to the appraised net asset value of Baoying Radio Factory as at 31 July 2001 pursuant to the asset appraisal report Su Ya Cheng Ping Bao Zi (2001) No.038 (蘇亞誠評報字(2001)第038號) prepared by Jiangsu Su Ya Jin Cheng Certified Public Accountants Co., Ltd. (江蘇蘇亞金誠會計師事務所有限公司) dated 31 August 2001. Under the preferential foreign investment policy of the People's Government of Baoying, the consideration payable by Yanlord Industrial in respect of the acquisition was reduced to RMB12.2 million and the approval with respect thereto was obtained from the relevant authority on 27 September 2001. Further, pursuant to the approval granted by the People's Government of Baoying on 23 October 2001, the remaining 20% of the Adjusted Net Assets of Baoying Radio Factory with a value of RMB2.8 million was awarded to 69 former employees of Baoying Radio Factory which, together with RMB800,000 provided by these former employees, would form the contributed capital of an enterprise, namely Baoying Hengda, which was set up for the purpose of forming joint venture with Yanlord Industrial.

On 1 November 2001, Baoying Renheng was established as a sino-foreign equity joint venture in the PRC with a registered capital of RMB18 million and a principal business scope of manufacturing machinery relating to tobacco, paper, chemical and light industrial products. The registered capital of Baoying Renheng was contributed as to RMB14.4 million by Yanlord Industrial by way of the Adjusted Net Assets of Baoying Radio Factory acquired as aforesaid and as to RMB3.6 million by Baoying Hengda by way of 20% of the Adjusted Net Assets of Baoying Radio Factory. Accordingly, the equity interests of Baoying Renheng were held as to 80% by Yanlord Industrial and as to 20% by Baoying Hengda.

On 23 July 2004, Zhuhai Mingtai, a company which is principally engaged in the production and sale of fine chemical products, entered into an equity transfer agreement with Baoying Hengda to acquire 20% equity interests in Baoying Renheng held by Baoying Hengda for a cash consideration of RMB6.8 million which was determined with reference to the then net asset value of Baoying Renheng attributable to Baoying Hengda. Zhuhai Mingtai is indirectly beneficially owned as to 95% by Mr. Wei and as to 5% by Ms. Liu. Pursuant to the said equity transfer agreement, Baoying Hengda undertook that it would not engage in any business relating to the tobacco industry after the signing of the agreement. On 11 August 2004, the transfer was approved by the relevant authority, subsequent to which Baoying Renheng was owned as to 80% by Yanlord Industrial and 20% by Zhuhai Mingtai.

HISTORY AND DEVELOPMENT

In August 2004, the registered capital of Baoying Renheng was increased by RMB24,857,142.86 to RMB42,857,142.86 which was solely contributed by Yanlord Industrial by way of cash of RMB10,457,142.86 and by capitalising an amount of RMB14,400,000 in the reserves and retained earnings of Baoying Renheng available for distribution to Yanlord Industrial as at 31 December 2003. As a result, Baoying Renheng was held as to 91.6% by Yanlord Industrial and 8.4% by Zhuhai Mingtai. Such increase in the registered capital was approved by Yangzhou Bureau of Foreign Trade and Economic Cooperation (揚州市對外貿易經濟合作局) on 18 August 2004.

In 2008, Mr. Zhong Sheng Jian decided to transfer his beneficial interests in Baoying Renheng to Mr. Wei and Ms. Liu as a gift. On 18 May 2008, Yanlord Industrial entered into a tripartite equity transfer agreement with Zhuhai Mingtai and Yanlord Industry Investment, a company incorporated in Hong Kong on 14 May 2005 and held as to 60% by Mr. Wei and 40% by Ms. Liu. Pursuant to the transfer agreement, Yanlord Industrial agreed to transfer its 91.6% interest in Baoying Renheng to Yanlord Industry Investment at nil consideration, and Zhuhai Mingtai agreed not to exercise its first right of refusal to acquire such equity interest. Subsequent to the disposal by Yanlord Industrial of its equity interests in Baoying Renheng, Mr. Zhong Sheng Jian and Yanlord Industrial have no shareholding relationship with our Group. The equity transfer was approved by Yangzhou Bureau of Foreign Trade and Economic Cooperation on 1 August 2008, subsequent to which all of the equity interests in Baoying Renheng are beneficially owned by Mr. Wei and Ms. Liu. Mr. Wei and Ms. Liu have confirmed that they do not have any understanding, express or implied, with Mr. Zhong Sheng Jian that they are required to take instruction from Mr. Zhong Sheng Jian in managing the business of the Company or in handling their investments in the Company.

On 15 October 2009, Renheng Global was incorporated in BVI with limited liability and was wholly-owned by Yanlord Industry Investment. Renheng Global was incorporated as an intermediate holding company of our Group's interest in Baoying Renheng.

For the purpose of reorganising the businesses held by Mr. Wei and Ms. Liu, on 28 October 2009, Renheng Tech, a wholly-owned subsidiary of Renheng Global, entered into a transfer agreement with Yanlord Industry Investment and Zhuhai Mingtai respectively to acquire their respective 91.6% and 8.4% equity interests in Baoying Renheng for nil consideration. The transfers were approved by Yangzhou Bureau of Foreign Trade and Economic Cooperation on 24 November 2009. Thereafter, Baoying Renheng became a wholly-owned subsidiary of Renheng Tech. Subsequently, on 25 November 2009, Baoying Renheng obtained the Certificate of Approval for Establishment of Enterprises with Investment of Taiwan, Hong Kong, Macao and Overseas Chinese in the PRC (中華人民共和國台灣港澳僑投資企業批准證書) and was converted from a Sino-foreign equity joint venture to a wholly foreign-owned enterprise.

On 2 February 2011, our Company was incorporated in the Cayman Islands as the holding company of our Group. As at the date of incorporation of our Company, the authorised share capital of our Company was HK\$387,500 divided into 38,750,000 shares of HK\$0.01 each.

HISTORY AND DEVELOPMENT

BUSINESS DEVELOPMENT

Since the incorporation of Baoying Renheng, our sole operating subsidiary, in November 2001, we have been engaged in the manufacture and sale of tobacco machinery by resuming the machinery manufacturing business originally conducted by Baoying Radio Factory. Mr. Wei was the legal representative and chairman of Baoying Renheng upon its incorporation and was responsible for the overall management as well as strategic planning of Baoying Renheng. On 15 January 2002, we obtained the Tobacco Production Licence under which we were permitted to manufacture and sell two types of catalogued special-purpose tobacco machinery products, namely PF system and PP system. Since then, Baoying Renheng has been focusing on the design and development, as well as production and sale of our major products, namely casing and flavouring system, PF system and PP system, as well as dedusting system. In 2002, our casing and flavouring system started to possess multiple functions including casing and flavour preparation, storage, pipeline delivery as well as spraying, and was equipped with a computerised system with control and fault diagnosis functions which significantly enhanced the overall capability of the casing and flavouring system as compared with previous generations of manual casing and flavouring systems manufactured by Baoying Radio Factory in the 1990s. Casing and flavouring system was not classified as a type of catalogued special-purpose tobacco machinery product until 2004.

As a recognition to the quality of our production process, Baoying Renheng received ISO 9001:2000 certification in August 2002 for its quality management system for the design, production and servicing of electrical system for tobacco cutting production line, casing and flavouring system and cut tobacco feeding system.

On 9 August 2003, Yanlord Industrial and the People's Government of Baoying entered into an agreement pursuant to which, among others, the People's Government of Baoying agreed to offer a new site in Baoying to Yanlord Industrial for relocation of the production facilities of Baoying Renheng whereas Yanlord Industrial agreed to revert the then production site of Baoying Renheng (including the Old Land and the facilities constructed thereon) to the People's Government of Baoying.

In May 2004, STMA issued the Tobacco Machinery List which took effect on 1 June 2004. Casing and flavouring system was added as a new type of catalogued special-purpose tobacco machinery product in the Tobacco Machinery List. On 10 August 2004, we successfully renewed our Tobacco Production Licence to include the manufacture and sale of casing and flavouring system.

In 2005, we relocated our production facilities to the New Land with a site area of approximately 62,741 sq.m. for which we have obtained the relevant State-owned land use rights certificate for industrial use for a term expiring on 6 June 2054. Under the preferential foreign investment policy of the People's Government of Baoying, Baoying Renheng was granted a refund of the full amount of the consideration payable for grant of land use rights of the New Land in the sum of RMB7,283,260.50. At the request of the local finance bureau of Baoying, Baoying Renheng and the local finance bureau mutually agreed that the consideration payable for grant of land use rights would be set off against the land refund granted by the People's Government of Baoying. As a result, Baoying Renheng did not make any direct payment in settling the land use rights premium of the New Land. As advised by the PRC Legal Advisers, (i) as the consideration payable for grant of land use rights was fully

HISTORY AND DEVELOPMENT

set off against the land refund, Baoying Renheng had fulfilled its payment obligation in respect of the acquisition of the relevant land use rights; and (ii) the respective written confirmations from the Bureau of Land and Resources of Baoying (寶應縣國土資源局) and the People's Government of Baoying dated 2 March 2011 and 28 March 2011 stated that the payment procedures regarding the consideration payable for grant of land use rights of the New Land were complete. The PRC Legal Advisers are of the view that Baoying Renheng possesses the land use rights of the New Land for the term of the relevant State-owned land use rights certificate (國有土地使用證). Under the interpretation of the relevant accounting standard applicable to the accounting period concerned, the acquisition of the land use rights of the New Land and the reversion of the Old Land to the People's Government of Baoying formed an exchange of dissimilar non-monetary assets. Accordingly, the New Land was accounted for as an asset and the land cost was recognised initially with reference to the fair value of the Old Land as at 6 June 2004, being the date of completion of the acquisition of the land use rights of the New Land. In addition, the refund of RMB7,283,260.50 was not accounted for in the financial statements of our Group in the year concerned. In June 2005, we completed the construction of the first phase of our production base with an aggregate gross floor area of approximately 11,183 sq.m. mainly used for production and offices. Following the completion of the second phase comprising a factory building and a dormitory building in September 2006, the aggregate gross floor area of our production base increased to approximately 26,986 sq.m..

In 2005, we successfully developed a new series of PF system that could reduce the possible damage to the processed cut tobacco. With the development of computer technology, in 2006, we introduced a computerised management system to our casing and flavouring system that is capable of storing the operating parameters of different cigarette recipes, automatically managing the blending of flavours and casings during the cigarette production process, integrating with other management systems such as manufacturing executive systems and enterprise resource planning systems in the exchange of data as well as analysing and executing production functions. In the same year, we enhanced the capability of our PP system by increasing the packing density of tobacco leaves.

With a view to enhancing automation of our production process and improving the quality of our products, in January 2006, we purchased a CNC press brake, a programmable machine tool, which has enhanced the accuracy of the bending angle and the quality of the bended metal sheet. In 2007, the new series of PF system developed by us in 2005 was launched and received favourable response from the cigarette manufacturers who then placed orders with our Group. We subsequently obtained the approval for the registration of two patents regarding this new PF system in the same year.

With our ability to cater to the needs of different cigarette manufacturers, we rolled out two new models of PF system in 2008, one of which can be deployed in high-speed cigarette production process.

During 2008, we developed and launched a new product, namely automated swelling agent delivery system, which is designed to deliver the swelling agent to the filter rod forming machine. The system can achieve the automatic delivery of the swelling agent although most of the cigarette manufacturers are still performing such function manually. We received favourable responses from our customers and secured several contracts to supply this product.

HISTORY AND DEVELOPMENT

In 2008, leveraging on our expertise in PF system, we successfully developed a new series of dedusting system with enhanced air stabilisation capabilities to meet the needs of cigarette manufacturers. The new dedusting system, installed with a newly designed air flow velocity detecting device as well as an automatic air flow adjusting device to reduce the breakage of tobacco and the blockage created by cut tobacco, is equipped with the PF system to facilitate the pneumatic feeding of processed cut tobacco, resulting in better control of the density of processed cut tobacco in each cigarette during the wrapping process to maintain the quality of the cigarettes.

We believe that automation is one of the major technical and product trends for the PRC tobacco machinery industry. Leveraging on our experience and expertise in casing and flavouring systems, we entered into a technical agreement with a cigarette manufacturer in July 2009 to develop a custom-made automated casing and flavouring system with additional automatic features for its cigarette factory in Shanghai. This new casing and flavouring system employs an automatic mechanical device in the storage, retrieval and feeding of semi-processed flavour and casing mixtures for the blending process, which limits the chance of human error in the process. We applied for the registration of 5 jointly owned patents with the relevant cigarette manufacturer regarding this casing and flavouring system in the PRC in September 2009 and have been granted approval for the registration of one of the patents in June 2010. We entered into an agreement with CTMC in May 2010 to supply this new casing and flavouring system to the relevant cigarette manufacturer after the relevant purchase approval document was issued by STMA. The installation and testing of this system have been completed in December 2010.

With our strong product development and customisation capabilities, we entered into a technical agreement with a cigarette manufacturer in February 2010 to design an automated casing and flavouring system to meet its new production needs. Based on the requirements of the cigarette manufacturer, the processing of casings and flavours has to be carried out in its central blending centre to standardise the taste and texture creation according to the recipes of individual cigarette brands. The processed flavour and casing mixtures are prepared without solvents and are therefore highly concentrated. With the traditional casing and flavouring system, the tanks are interconnected and all ingredients enter into a pipeline from the storage tanks for delivery to the blending tank. This process would incur raw material loss during the pipeline delivery of the concentrated flavour and casing mixtures to the blending tank. In order to reduce the loss of raw materials during the pipeline delivery in the preparation of concentrated mixtures at the central blending centre, we have developed a tailored-made automated casing and flavouring system where individual ingredients are fed directly to movable tanks which will be transported on a conveyor belt to the blender. The processed mixtures will then be distributed to different cigarette production sites of the cigarette manufacturing group. In March 2010, we applied for the registration of two jointly owned patents with the relevant cigarette manufacturer regarding this casing and flavouring system in the PRC. In April 2010, we entered into an agreement with CTMC to supply this new casing and flavouring system to the cigarette factory of the relevant cigarette manufacturer in Kunming after the relevant purchase approval document was issued by STMA. We also contracted directly with this cigarette manufacturer to supply other components and devices which are not listed in all of the Tobacco Machinery Documents but form integral part of this customised system. The part of this project contracted with CTMC was completed in May 2011, while the remaining part of this project is expected to be completed in November 2011.

HISTORY AND DEVELOPMENT

To improve the quality of metal tube-welding during our production process, we acquired an automatic pipeline welding machine in October 2010 which can be used in the welding of the piping system in our casing and flavouring system.

We are committed to continuously improving and upgrading our production quality, facilities and production techniques. Over the years, we have been granted or accredited a number of awards and certifications by various governmental authorities in the PRC in recognition of our industry standing and product quality. These included Advanced Technological Work Unit (企業科技工作先進單位) awarded by the People's Government of Baoying in 2003, the High and New Technology Enterprise Certificate (高新技術企業認定證書) issued by JSTD in 2005, and the Award of Automatic Tobacco-related Casing and Flavouring System (煙用糖料香料自動調配及自動加香加料裝置獲獎證書) awarded by the People's Government of Yangzhou (揚州市人民政府) in 2006. As at the Latest Practicable Date, we have obtained 5 solely owned patents as well as 2 jointly owned patents in the PRC and have applied for the registration of 8 jointly owned patents regarding our tobacco machinery products in the PRC.

In late 2010, through our established business relationship with a cigarette manufacturer in the PRC, we identified a new business opportunity in the PRC cigarette packaging industry. On 23 December 2010, we entered into a contract with an Independent Third Party, which was engaged in the sale of packaging material products, to supply hot stamped foil used in cigarette packaging. We sourced the hot stamped foil from a supplier, an Independent Third Party, which directly delivered the products to our customer in December 2010. During the six months ended 30 June 2011, we sourced our hot stamped foil from three suppliers, which were all Independent Third Parties, and sold our products to two customers. Although our Directors believe that the new hot stamped foil trading business will provide another source of income to our Group, it is not our current intention to establish this trading business as part of our core business. As at the Latest Practicable Date, the hot stamped foil trading business was only at an infancy stage and we did not have any concrete plan regarding the development of this new business.

THE REORGANISATION

We underwent the Reorganisation to rationalise our structure in preparation for the Listing. The Reorganisation involved the following:

(a) Change of names to Renheng Global and Renheng Tech

To streamline the English company names within our Group, on 21 December 2010, the English name of Yanlord Global Limited was changed to Renheng Global and on 28 December 2010 the English name of Yanlord Tech Limited was changed to the Renheng Tech with their respective Chinese names remain unchanged.

HISTORY AND DEVELOPMENT

(b) Incorporation of BVI companies by Mr. Wei and Ms. Liu

- (i) On 1 July 2010, LinkBest was incorporated in the BVI, with an authorised share capital of US\$50,000 divided into 50,000 shares of US\$1.00 each. On 7 December 2010, LinkBest issued 100 ordinary shares, being the entire issued share capital of the company, to Mr. Wei and Mr. Wei became its sole shareholder.
- (ii) On 8 October 2010, Open Venture was incorporated in the BVI, with an authorised share capital of US\$50,000 divided into 50,000 shares of US\$1.00 each. On 7 December 2010, Open Venture issued 100 ordinary shares, being the entire issued share capital of the company, to Ms. Liu and Ms. Liu became its sole shareholder.
- (iii) On 15 December 2010, LinkBest and Open Venture, respectively entered into a sale and purchase agreement with Yanlord Industry Investment to purchase 30,000 and 20,000 issued shares of Renheng Global, being the entire issued share capital of Renheng Global. Upon completion of the sale and purchase of Renheng Global on 15 December 2010, Renheng Global was held as to 60% and 40% by LinkBest and Open Venture.

(c) Incorporation of our Company

- (i) On 2 February 2011, our Company was incorporated in the Cayman Islands with an authorised share capital of HK\$387,500 divided into 38,750,000 shares of HK\$0.01 each to act as the ultimate holding company of our Group.
- (ii) On 2 February 2011, 60 subscriber Shares were allotted and issued as fully paid to LinkBest.
- (iii) On 2 February 2011, LinkBest and Open Venture entered into a share swap agreement with our Company (the “Share Swap Agreement”). Pursuant to the Share Swap Agreement, LinkBest and Open Venture transferred 30,000 and 20,000 issued shares of Renheng Global to our Company respectively by way of share swap in consideration and exchange of the Company issuing and allotting 60 and 40 Shares at par, credited as fully paid, to LinkBest and Open Venture, respectively.
- (iv) On 2 February 2011, our Company allotted and issued 40 shares to Open Venture credited as fully paid.
- (v) As a result of the above, a total of 60 (60%) and 40 (40%) Shares had been acquired by or issued to LinkBest and Open Venture, respectively.
- (vi) Upon completion of the above, LinkBest and Open Venture became the holding companies of our Company and Renheng Global became the direct wholly-owned subsidiary of our Company.

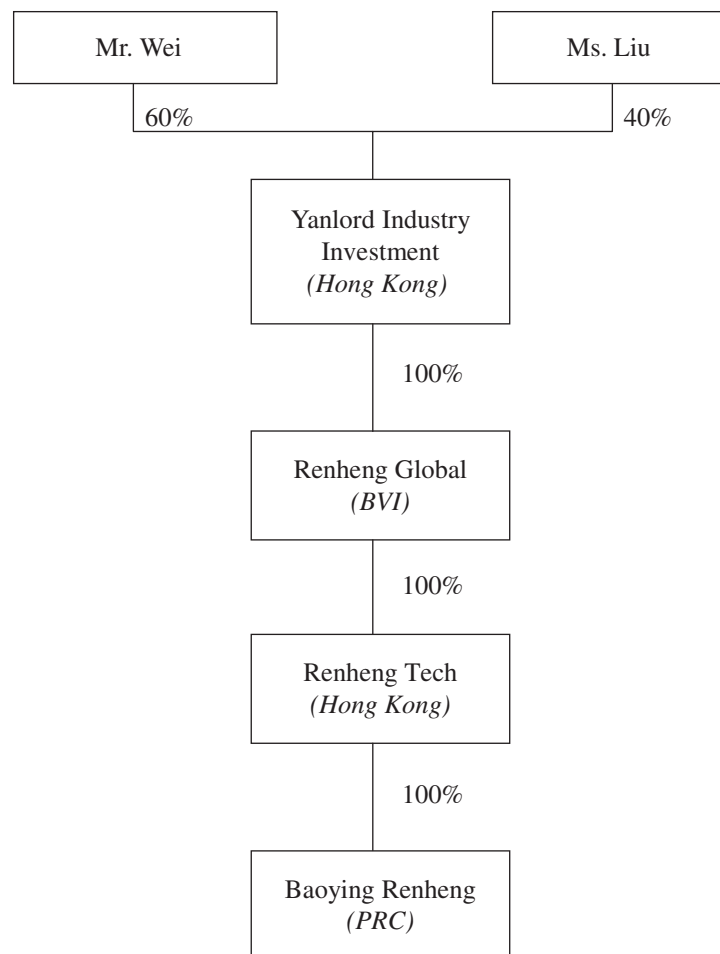
HISTORY AND DEVELOPMENT

(d) Capitalisation Issue

- (i) In order to achieve the percentage shareholding in our Company after the Listing, the Capitalisation Issue will be made, further details of which are set out under item (d) of paragraph B headed “Changes in share capital of the Company” in Appendix V to this prospectus.
- (ii) Upon completion of the Capitalisation Issue (but taking into no account of any Shares which may be issued upon the exercise of the options that has been granted under the Pre-IPO Share Option Scheme and may be granted under the Share Option Scheme), our Company will be held as to 45%, 30% and 25% by LinkBest, Open Venture and the public respectively.

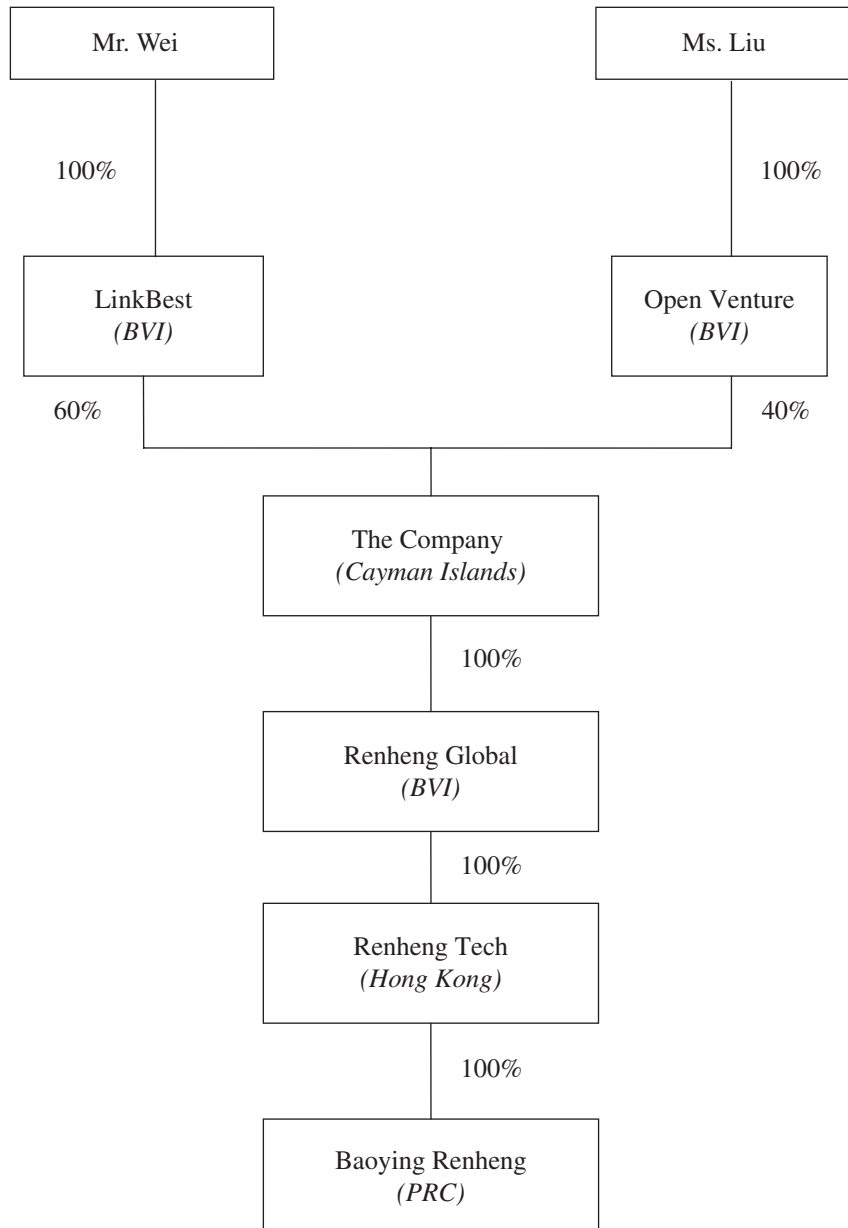
GROUP STRUCTURE

The following chart sets out the shareholding and corporate structure of our Group immediately prior to the Reorganisation:



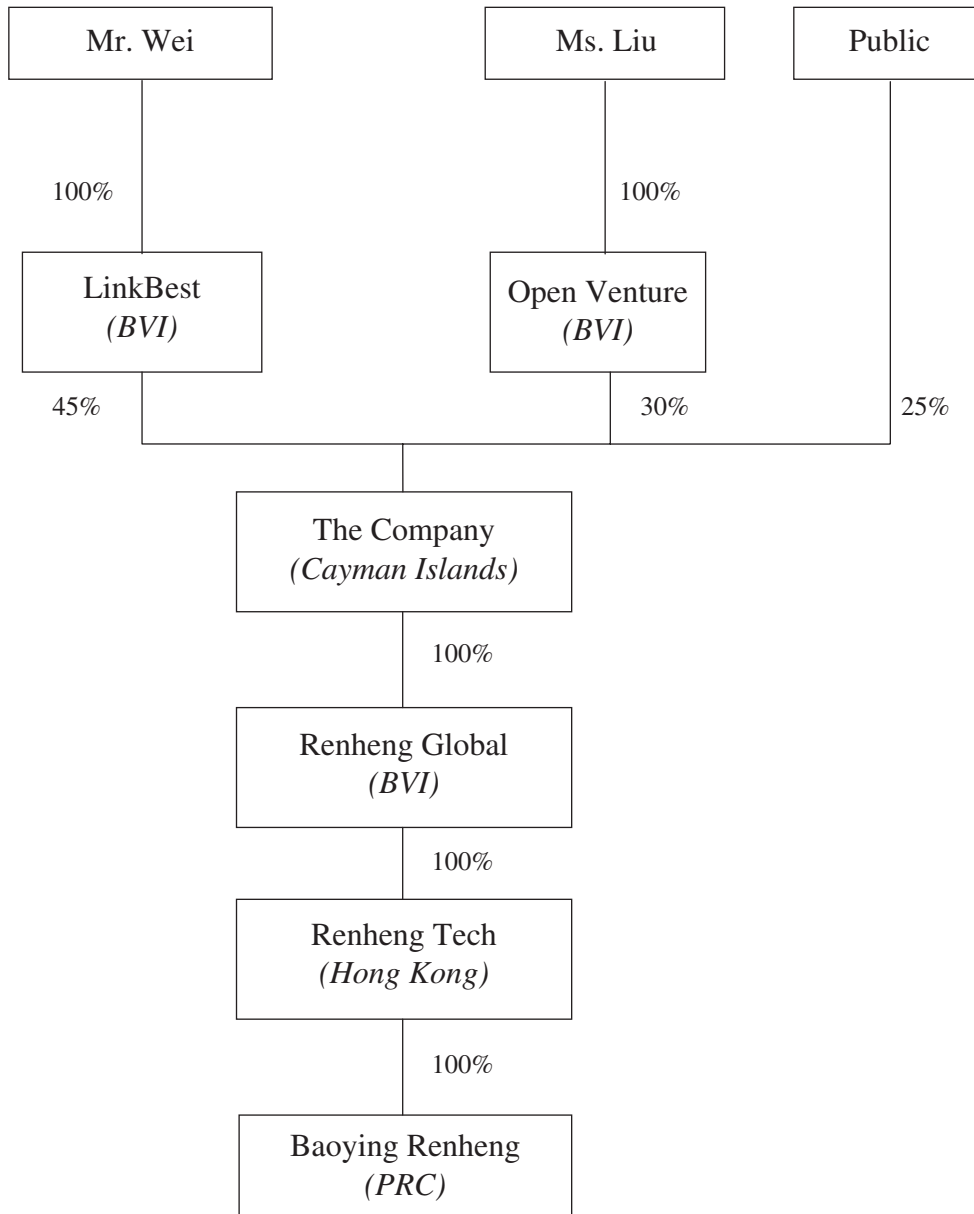
HISTORY AND DEVELOPMENT

The following chart sets out the shareholding and corporate structure of our Group after the Reorganisation and immediately before the Placing:



HISTORY AND DEVELOPMENT

The following chart sets out the shareholding and corporate structure of our Group immediately following the completion of the Placing:



HISTORY AND DEVELOPMENT

PRC GOVERNMENT APPROVALS

Pursuant to Notice 75 promulgated on 21 October 2005, PRC residents should register with the local branch of SAFE before establishing or controlling a privately held overseas special purpose vehicle for the purpose of overseas equity financing (including convertible debt financing). Further, when a PRC resident contributes the assets of or its equity interest in a domestic enterprise into an overseas special purpose vehicle, or engages in overseas financing after contributing assets or equity interest into an overseas special purpose vehicle, such PRC resident shall register his or her interest in the overseas special purpose vehicle and the change thereof with the local branch of SAFE. According to Notice 75, a domestic resident natural person refers to a natural person who holds a resident identity card of the PRC, a passport or other lawful identity certificates, or a natural person who has no legal identity in the PRC but habitually resides in the PRC due to reasons of financial interests. As advised by the PRC Legal Advisers, Mr. Wei and Ms. Liu do not fall within the definition of domestic resident natural person as set out in Notice 75 and such notice does not apply to them accordingly.

On 8 August 2006, the Ministry of Commerce, the State Assets Supervision and Administration Committee (國務院國有資產監督管理委員會), the State Taxation Bureau (國家稅務總局), the State Administration of Industry and Commerce (國家工商行政管理總局), the China Securities Regulatory Committee (中國證券監督管理委員會) and SAFE jointly issued the Foreign Investors M&A Rules. The Foreign Investors M&A Rules require that an application shall be made to the Ministry of Commerce for examination and approval of the acquisition of any company inside China affiliated with a domestic company, enterprise or natural person, which is made in the name of an overseas company lawfully established or controlled by such domestic company, enterprise or natural person. The Foreign Investors M&A Rules also provide that the overseas listing of a special purpose company controlled directly or indirectly by the PRC companies or individuals on an overseas stock market must be approved by the China Securities Regulatory Committee.

As advised by the PRC Legal Advisers, the Placing and the Listing do not require the approval of the China Securities Regulatory Committee or other relevant PRC government authorities as (i) our Company is a foreign enterprise established by foreign investors; (ii) our Company is not a domestic enterprise; and (iii) our Company is not an offshore special purpose company formed for listing purposes and controlled directly or indirectly by PRC companies or individuals. Therefore, the PRC Legal Advisers are of the view that the Guideline Regarding Domestic Enterprises Directly or Indirectly Seeking for Foreign Listings (境內企業直接或間接到境外發行證券或者將其證券在境外上市交易) promulgated by the China Securities Regulatory Committee or the Foreign Investors M&A Rules do not apply to our Company in respect of the Placing and the Listing.

BUSINESS

OVERVIEW

We are principally engaged in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of tobacco machinery products in the PRC. We generate our turnover primarily from projects related to three types of catalogued special-purpose tobacco machinery products as listed in the Tobacco Machinery Documents, namely casing and flavouring systems, PF systems and PP systems, and related components and devices not listed in all of the Tobacco Machinery Documents, which accounted for approximately 92.6%, 95.4% and 93.0% of our turnover for each of the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively.

In providing our catalogued special-purpose tobacco machinery products as listed in all of the Tobacco Machinery Documents, we enter into contracts directly with CTMC. Furthermore, in order to meet the functional specification of our end customers, we may also contract with end customers directly to supply components and/or devices which are not listed in all of the Tobacco Machinery Documents but form integral parts of the customised systems. These components and devices included, but were not limited to, conveyer structures, automated filling devices, automated dosing devices, filling valves, control units of blending, filling and rinsing, and mechanical items such as stirrers and drive dogs. Having considered that these components and devices (i) are not standalone systems as defined in the Tobacco Machinery List; and (ii) are not listed in the Pricing Guidelines or Pricing Approval 2010, the PRC Legal Advisers are of the opinion that those components and devices should not be classified as catalogued special-purpose tobacco machinery and the requirements pursuant to the Measures on Administration of Procurement are not applicable to the sales of these items, and hence such transactions with our end customers during the Track Record Period were not in breach of the relevant PRC laws and regulations.

Under the relevant PRC regulations, domestic manufacturers engaging in the production of tobacco machinery as listed on the Tobacco Machinery List must possess the Tobacco Production Licence to manufacture and sell the relevant tobacco machinery. The Tobacco Machinery List sets out 22 types of catalogued special-purpose tobacco machinery deployed in the production of tobacco products in the PRC and the Pricing Guidelines specify the guidance price of different models of catalogued special-purpose tobacco machinery products, whereas the Pricing Approval 2010 sets out the guidance price of various models of casing and flavouring systems not specified in the Pricing Guidelines. We have obtained a Tobacco Production Licence under which we are permitted to manufacture, sell and provide maintenance, overhaul as well as modification services in respect of casing and flavouring systems, feeding systems and PP systems. According to the China Tobacco Year Book 2009 published by STMA in December 2010, as at the end of 2009, there were 34 tobacco machinery manufacturers which have been granted the Tobacco Production Licence for the manufacture and sale of various types of catalogued special-purpose tobacco machinery.

We are also engaged in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of non-catalogued ancillary tobacco machinery products and services, which mainly include dedusting systems and swelling agent delivery systems.

BUSINESS

Our turnover of catalogued special-purpose tobacco machinery projects includes that derived from sales of three types of catalogued special-purpose tobacco machinery products and parts as well as sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents and are not contracted with CTMC but form integral parts of the customised systems. The following table sets forth a breakdown of our turnover by project category during the Track Record Period:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Catalogued special-purpose tobacco machinery projects								
Sales of tobacco machinery and parts/components/devices (<i>Note i</i>)								
Casing and flavouring systems	37,873	52.2	48,097	52.5	16,982	66.5	55,237	85.4
PF systems	10,545	14.5	13,790	15.0	5,215	20.4	936	1.5
PP systems	4,858	6.7	2,381	2.6	–	–	–	–
	<u>53,276</u>	<u>73.4</u>	<u>64,268</u>	<u>70.1</u>	<u>22,197</u>	<u>86.9</u>	<u>56,173</u>	<u>86.9</u>
Provision of maintenance, overhaul and modification services								
Casing and flavouring systems	11,288	15.5	13,091	14.3	769	3.0	2,137	3.3
PF systems	1,854	2.6	4,015	4.4	1,192	4.7	1,540	2.4
PP systems	805	1.1	6,095	6.6	510	2.0	273	0.4
	<u>13,947</u>	<u>19.2</u>	<u>23,201</u>	<u>25.3</u>	<u>2,471</u>	<u>9.7</u>	<u>3,950</u>	<u>6.1</u>
Sub-total								
Casing and flavouring systems	49,161	67.7	61,188	66.8	17,751	69.5	57,374	88.7
PF systems	12,399	17.1	17,805	19.4	6,407	25.1	2,476	3.9
PP systems	5,663	7.8	8,476	9.2	510	2.0	273	0.4
	<u>67,223</u>	<u>92.6</u>	<u>87,469</u>	<u>95.4</u>	<u>24,668</u>	<u>96.6</u>	<u>60,123</u>	<u>93.0</u>
Other projects and products								
Sales of non-catalogued ancillary tobacco machinery (<i>Note ii</i>)								
	1,636	2.2	2,125	2.3	–	–	2,286	3.5
Provision of maintenance, overhaul and modification services								
	3,757	5.2	498	0.5	870	3.4	–	–
Sales of hot stamped foil products								
	–	–	1,621	1.8	–	–	2,242	3.5
	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Sub-total								
	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Total								
	<u>72,616</u>	<u>100.0</u>	<u>91,713</u>	<u>100.0</u>	<u>25,538</u>	<u>100.0</u>	<u>64,651</u>	<u>100.0</u>

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- Notes:* (i) Turnover of catalogued special-purpose tobacco machinery projects contracted with CTMC amounted to approximately HK\$53,208,000, HK\$60,589,000 and HK\$21,893,000, representing approximately 73.3%, 66.1% and 33.9% of our total turnover during the Track Record Period. Turnover generated from catalogued special-purpose tobacco machinery projects also includes that derived from sales of parts and sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents and are not contracted with CTMC but form integral parts of the customised systems, which amounted to approximately HK\$68,000, HK\$3,679,000 and HK\$34,280,000, representing 0.1%, 4.0 % and 53.0% of our total turnover respectively during the Track Record Period. Despite the separate sale and purchase agreement, as these components and/or devices were included in the technical specification of the corresponding catalogued special-purpose tobacco machinery projects and cannot function separately from the catalogued special-purpose tobacco machinery system, the revenue derived from the sales of these items is classified under the relevant category of catalogued special-purpose tobacco machinery projects. The significant increase in the sales of these components and/or devices during the six months ended 30 June 2011 was mainly attributable to substantial turnover recognised from the customised casing and flavouring system with movable tanks project with our customer in Kunming during the period. For further details, please refer to the paragraph headed “Description of selected consolidated statement of comprehensive income line items – Turnover” under the “Financial information” section in this prospectus.
- (ii) Non-catalogued ancillary tobacco machinery products mainly comprised dedusting systems and swelling agent delivery systems.

We conduct our tobacco machinery product business on a project basis and all of our products are custom-made to meet the needs of cigarette manufacturers and tobacco redrying factories in the PRC.

COMPETITIVE STRENGTHS

Well established and proven development and customisation capabilities

Our Directors believe that our well established and proven development and customisation capabilities have enabled our Group to capture new business opportunities and develop new products to meet the requirements of cigarette manufacturers and tobacco redrying factories in various projects. For instance, we were able to develop a custom-made casing and flavouring system with additional automatic logistic features for a project with a cigarette manufacturer in Shanghai. We applied for the registration of 5 jointly owned patents with this cigarette manufacturer regarding the said casing and flavouring system in the PRC in September 2009 and have been granted approval for the registration of one of the patents in June 2010. With the support of our own technical department, we are able to respond to the requests of cigarette manufacturers and tobacco redrying factories in a timely manner. Our technical department is actively involved in the design stage with our customers to optimise product features and functions and to provide substantial input and support to the product design and development process of our projects.

Commitment to product quality

Our Group is committed to designing and manufacturing products with high quality standards. Our quality control department is responsible for implementing quality control measures and monitoring quality control procedures. We have adopted quality control and assurance procedures throughout our production process, from the sourcing of raw materials, parts and components to the production

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processes. Further details are set out in the paragraph headed “Quality control” in this section. As a recognition to the quality of our production process, we have been awarded ISO 9001:2008 certification for our quality management system for the design, production and sales of electrical systems for tobacco cutting production line, casing and flavouring system and cut tobacco feeding system. As a result of our stringent quality control system, we have not experienced any product complaint or return due to product quality problems up to the Latest Practicable Date.

Long standing relationships with cigarette manufacturers and tobacco redrying factories

We have established close business relationships with cigarette manufacturers and tobacco redrying factories in the PRC with our ability to develop customised tobacco machinery and our commitment to delivering high quality products. Save for two of our five largest end customers for the six months ended 30 June 2011, which began their business relationship with us during the period, the remaining of our five largest end customers for the Track Record Period have maintained business relationships with us for periods ranging from 2 to 9 years. Our marketing personnel regularly visit the cigarette manufacturers and tobacco redrying factories to collect market information as well as to identify potential projects, and our technical department works closely with our customers to develop products that meet their specific needs in various projects. Such long standing relationships with the major cigarette manufacturers and tobacco redrying factories are critical to the success of our business.

Experienced management team

Our senior management team has extensive experience in the tobacco machinery manufacturing industry or engineering business. Mr. Wei, chairman of our Board, has more than 14 years of experience in the electrical and mechanical equipment industry. Mr. Sun Zhaohui, one of our executive Directors the chief executive officer of our Company and the legal representative of Baoying Renheng, has no less than 10 years of engineering experience. Mr. Xu Jiagui, a director and general manager of Baoying Renheng, has over 8 years of research and development, production and general management experience relating to the tobacco machinery manufacturing industry. Mr. An Zhanqi, the chief engineer of Baoying Renheng, has no less than 9 years of experience in the engineering field. We believe that the experience and commitment of our senior management team are key to our success.

BUSINESS MODEL

We conduct our tobacco machinery product business on a project basis and all of our products are custom-made to meet the needs of cigarette manufacturers and tobacco redrying factories in the PRC.

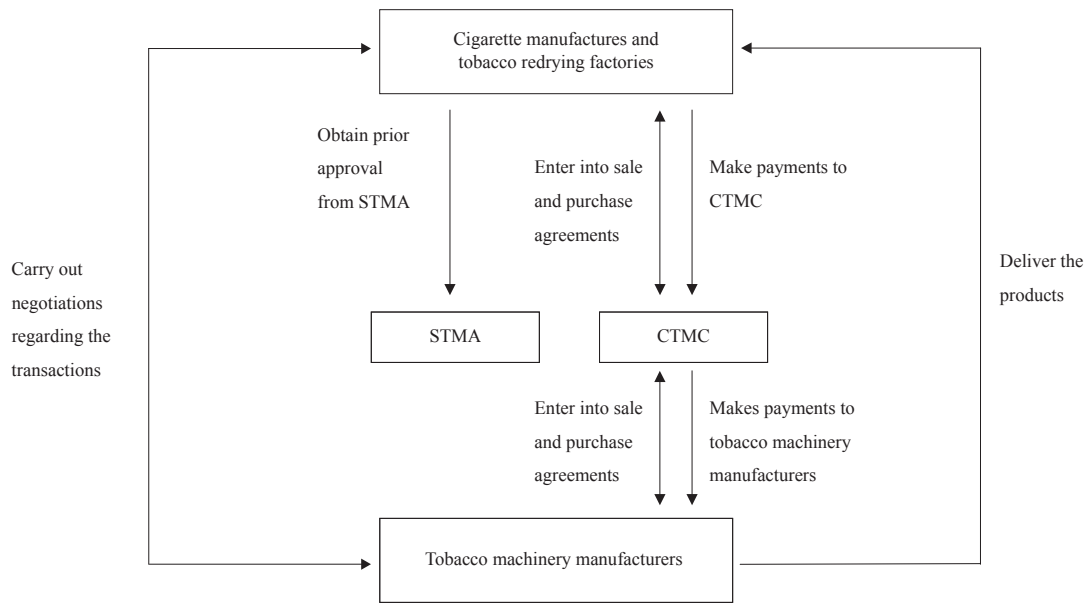
We are principally engaged in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of tobacco machinery products in the PRC. We generate our turnover primarily from projects related to three types of catalogued special-purpose tobacco machinery products as listed in the Tobacco Machinery Documents, namely casing and flavouring systems, PF systems and PP systems, and related components and devices not listed in all of the Tobacco Machinery Documents, which accounted for approximately 92.6%, 95.4% and 93.0% of our turnover for each of the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively.

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Under the relevant PRC regulations, domestic manufacturers engaging in the production of tobacco machinery as listed on the Tobacco Machinery List must possess the Tobacco Production Licence to manufacture and sell the relevant tobacco machinery. The Tobacco Machinery List, which was issued by STMA on 24 May 2004 and became effective on 1 June 2004, sets out 22 types of catalogued special-purpose tobacco machinery deployed in the production of tobacco products in the PRC and the Pricing Guidelines were issued by STMA and specify the guidance price of different models of catalogued special-purpose tobacco machinery products, whereas the Pricing Approval 2010 was issued by STMA on 22 April 2010 as additional supplement to the Pricing Guidelines and it sets out the guidance price of various models of casing and flavouring systems not specified in the Pricing Guidelines. We have obtained a Tobacco Production Licence under which we are permitted to manufacture, sell and provide maintenance, overhaul as well as modification services in respect of casing and flavouring systems, feeding systems and PP systems. Our Tobacco Production Licence remains valid as at the Latest Practicable Date.

Pursuant to the Measures on Administration of Procurement, procurements of catalogued special-purpose tobacco machinery listed on the Tobacco Machinery List must be approved by STMA in advance. In addition, pursuant to these regulations, CTMC, being a subsidiary unit of CNTC, monitors and oversees all domestic made catalogued special-purpose tobacco machinery procurement matters between the tobacco machinery manufacturers and the cigarette manufacturers in the PRC. The PRC Legal Advisers are of the opinion that catalogued special-purpose tobacco machinery refers to (i) standalone system set out on the Tobacco Machinery List, which is defined as tobacco machinery which is able to complete one or more specific processes and is independently operated in the production and processing of tobacco raw materials and auxiliary materials; and (ii) tobacco machinery products specifically listed in the Pricing Guidelines and Pricing Approval 2010.

The arrangements under the relevant regulatory requirements in respect of procurements of catalogued special-purpose machinery are illustrated in the diagram below:



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CTMC acts as a government agency to fulfill the relevant regulatory requirements in the procurement arrangements and is not involved in the negotiations regarding the transactions which are carried out between the tobacco machinery manufacturers and the purchasers. CTMC, when acting as the buyer, places order with tobacco machinery manufacturers to purchase catalogued special-purpose tobacco machinery products, and when acting as the vendor, supplies such tobacco machinery products to tobacco industrial enterprises (including cigarette manufacturers and tobacco redrying factories). As such, CTMC enters into sale and purchase agreements with us in connection with machinery procurements made by cigarette manufacturers and tobacco redrying factories with the instructions to deliver our special-purpose machinery products to the designated cigarette manufacturers and tobacco redrying factories. The following summarises the major contractual terms of the typical sale and purchase agreements entered into between our Group and CTMC:

- **Payment terms.** CTMC is required to make an initial payment of 20% of the contract value in 2 months after signing the sale and purchase agreement, 70% of the contract value upon receipt of the signed delivery note from the end customer and the sales invoice issued by our Group, and the remaining 10% as warranty retention money to be released upon submission of the original acknowledgement of inspection. No timeframe for the submission of the original acknowledgement of inspection by us to CTMC is stipulated in the sale and purchase agreement. As advised by the PRC Legal Advisers, CTMC, being a party to the sale and purchase agreement, is responsible for making payment to our Group pursuant to the terms of the agreement and such payment is not subject to the fulfillment of the payment obligation by the end customers to CTMC.

During the Track Record Period, we would generally receive the original acknowledgement of inspection which was dated within an average of 8 months from the completion of the project. Furthermore, we generally received the retention money from CTMC within an average of 3 months from the date of the original acknowledgement of inspection signed by us and the end customer.

- **Delivery.** We are required to deliver our catalogued special-purpose tobacco machinery to the designated cigarette manufacturers or tobacco redrying factories on or before the delivery deadline specified in the sale and purchase agreement. We will deliver our catalogued special-purpose tobacco machinery products to the end customers after receipt of the delivery note issued by CTMC and the delivery permit issued by STMA or its authorised agencies.
- **Quality.** We shall ensure that the quality of our tobacco machinery products complies with the industry standards and offer after-sales support.

Our Directors confirmed that, during the Track Record Period and up to the Latest Practicable Date, except for the postponement in the delivery schedule requested by our end customers, neither our Group nor CTMC had breached the terms of the sale and purchase agreements.

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As advised by the PRC Legal Advisers, the end customers have no obligation to settle the payment directly with our Group given that CTMC acts as the buyer of our catalogued special-purpose tobacco machinery and enters into the sale and purchase agreement with our Group. Pursuant to 國家煙草專賣局關於印發《煙草專用機械產品購銷合同管理辦法》的通知 (the Notice of STMA on Issuing the Measures on Administration of Sale and Purchase Contracts of Catalogued Special-purpose Tobacco Machinery) (GUO YAN FA [1996] No.27), (i) CTMC will issue the delivery note to the tobacco machinery manufacturers after receiving payment from the purchasers pursuant to the terms of the relevant sale and purchase contracts; and (ii) the tobacco machinery manufacturers will deliver the products to the end customers after receipt of the delivery note from CTMC and delivery permit from STMA or its authorised agencies. To the best of our Directors' knowledge, the end customers have to settle their payments with CTMC before the delivery of products by our Group to the end customers. Our Directors consider that our Group is not in a position to ensure that CTMC will not hold up the amount settled by the end customers. However, the Group has not, up and until the Latest Practicable Date, encountered any delay or default in payment by CTMC. The PRC Legal Advisers have advised that if we have delivered the products to the end customers but the end customers fail to pay CTMC, CTMC is still responsible for making payment to us after our submission of the sales invoice as well as the delivery note and original acknowledgement of inspection signed by the end customers. In the event that CTMC fails to make payment to us according to the terms of the sale and purchase agreement, we are entitled to claim payment from CTMC under relevant PRC law.

Since the incorporation of Baoying Renheng and up to the Latest Practicable Date, our Group paid handling fee to CTMC for each type of catalogued special-purpose machinery products at 3% of the value of the contracts entered into between our Group and CTMC. The amounts were not paid separately by us, but were deducted by CTMC directly from its progress payments made to our Group.

Notwithstanding the aforesaid regulations, in order to meet the functional specification of our end customers, our custom-made systems may also be equipped with components and/or devices which are not listed in all of the Tobacco Machinery Documents but form integral parts of the customised systems. In such cases, our end customers may enter into a separate sale and purchase agreement with us for such components and/or devices, which is supplemental to the sale and purchase agreement entered into between our Group and CTMC. These components and devices included, but were not limited to, conveyer structures, automated filling devices, automated dosing devices, filling valves, control units of blending, filling and rinsing, and mechanical items such as stirrers and drive dogs equipped with the customised casing and flavouring system with movable tanks. A brief description of these components and devices is set out as follows:

- conveyer structures – the skeleton of the system to transport the movable tanks for the respective production processes such as filling and blending, which replace the interconnecting pipelines under the traditional casing and flavouring system
- automated filling and dosing devices – the full set of system to handle the mixing of more than 200 types of casings and flavours and perform the automatic filling of casings and flavours stored in the raw material storage tanks into the movable tanks, which help to increase the precision and reduce wastage as compared to the traditional casing and flavouring systems

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- filling valves – devices equipped with and compatible with the automatic filling devices that regulate, direct and control the flow of the casings and flavours
- control units of blending, filling and rinsing – software sourced from an independent supplier to control the blending, filling and rinsing processes for the movable tanks
- stirrers and drive dogs – the mechanical items to link the movable tanks and the system for the blending process

The types of components and devices may vary depending on the specifications and requirements of our end customers.

Having considered that these components and devices (i) are not standalone systems as defined in the Tobacco Machinery List; and (ii) are not listed in the Pricing Guidelines or Pricing Approval 2010, the PRC Legal Advisers are of the opinion that those components and devices should not be classified as catalogued special-purpose tobacco machinery and the requirements pursuant to the Measures on Administration of Procurement are not applicable to the sales of these items, and hence such transactions with our end customers during the Track Record Period were not in breach of the relevant PRC laws and regulations. During the Track Record Period, sales of these components and/or devices amounted to approximately HK\$68,000, HK\$3,679,000 and HK\$34,280,000 respectively. The significant increase in the sales of these component and/or devices during the six months ended 30 June 2011 was mainly attributable to substantial turnover recognised from the customised casing and flavouring system with movable tanks project with our customer in Kunming during the period. For further details, please refer to the paragraph headed “Description of selected consolidated statement of comprehensive income line items – Turnover” under the “Financial information” section of this prospectus.

The following summarises the major contractual terms of the sale and purchase agreement entered into between our Group and our customers of catalogued special-purpose tobacco machinery projects other than CTMC:

- **Payment terms:** The customers are generally required to make an initial deposit of 10% to 30% of the contract value after signing the sale and purchase agreement, and to pay up to 90% to 95% of the contract value upon completion of projects, delivery of products or acceptance of products as agreed with the customer on case-by-case basis. The remaining balance will be payable by the customer upon the expiration of the warranty period ranging from 1 to 2 years.
- **Delivery:** We are required to deliver the parts and components on or before the delivery deadline specified in the sale and purchase agreement.
- **Quality:** We shall ensure that the quality of our tobacco machinery products complies with the technical agreement signed with the customer.
- **Packaging:** We shall be responsible for the packaging and adopt measures to prevent moisture, sunlight, rust, corrosion and damage from physical impact during the delivery process.

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Our Directors confirmed that, during the Track Record Period and up to the Latest Practicable Date, except for the postponement in the delivery schedule requested by our end customers, neither our Group nor our customers of catalogued special-purpose tobacco machinery projects had breached the terms of the sale and purchase agreements.

For the provision of maintenance, overhaul and modification services in respect of our catalogued special-purpose tobacco machinery products, we enter into service contracts with the cigarette manufacturers and the tobacco redrying factories directly.

We are also engaged in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of non-catalogued ancillary tobacco machinery products and services, which mainly include dedusting systems and swelling agent delivery systems. In providing such products and services, we enter into contracts directly with the cigarette manufacturers.

By virtue of our contractual relationship with CTMC under the aforesaid regulatory requirements in respect of the sale of catalogued special-purpose tobacco machinery, CTMC was our largest customer during the two years ended 31 December 2010 and was our second largest customer for the six months ended 30 June 2011, and accounted for approximately 73.3% and 66.1% and 33.9% of our turnover for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. Nevertheless, the end customers of our catalogued special-purpose tobacco machinery are normally cigarette manufacturers (in the case of our casing and flavouring systems and PF systems) and tobacco redrying factories (in the case of our PP systems). The remaining portion of our revenue during the Track Record Period was derived from the sale of our non-catalogued ancillary tobacco machinery products, the sale of tobacco machinery parts, components and devices, and the provision of maintenance, overhaul and modification services in respect of both catalogued special-purpose tobacco machinery and non-catalogued ancillary tobacco machinery to cigarette manufacturers and tobacco redrying factories. As advised by the PRC Legal Advisers, these businesses are not subject to the relevant requirements in respect of the sale of catalogued special-purpose tobacco machinery under the Measures on Administration of Procurement and accordingly, we can enter into contracts directly with our customers. The PRC Legal Advisers are of the opinion that our Group's transactions with the customers other than CTMC are not in breach of the relevant PRC laws and regulations.

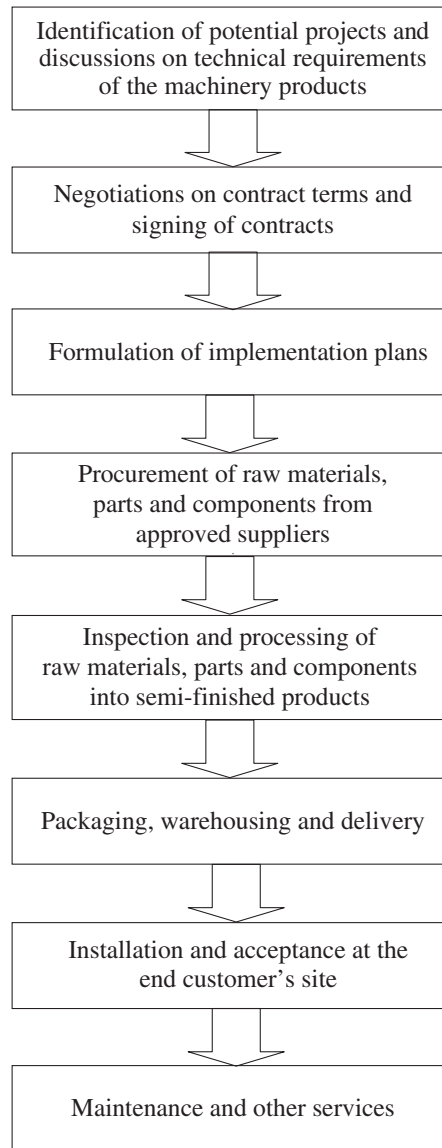
The value of our tobacco machinery projects varies depending on the types and complexity of the products and services provided. The following table sets forth an analysis of the aggregate contract value by project category for contracts completed during the Track Record Period.

Contract value (RMB)	Year ended 31 December 2009				Year ended 31 December 2010				Six months ended 30 June 2011						
	Casing and flavouring systems		PF systems	PP systems	Others	Casing and flavouring systems		PF systems	PP systems	Others	Casing and flavouring systems		PF systems	PP systems	Others
5 million or above	61.8%	-	-	-	73.6%	-	-	-	81.9%	-	-	-	-	-	-
1 million or above but less than 5 million	26.8%	51.4%	85.8%	22.3%	19.4%	76.9%	79.1%	67.5%	5.3%	43.1%	-	-	-	30.4%	
Less than 1 million	11.4%	48.6%	14.2%	77.7%	7.0%	23.1%	20.9%	32.5%	12.8%	56.9%	100.0%	100.0%	100.0%	69.6%	
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	

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PROJECT OPERATION PROCESS

The following chart sets out the project operation process for our tobacco machinery product business:



(i) Identification of potential projects and discussions on technical requirements of the machinery products

Our sales and marketing team pays regular visits to domestic cigarette manufacturers and tobacco redrying factories to collect market information and identify business opportunities. We identify potential projects through either business discussions with domestic cigarette manufacturers as well as tobacco redrying factories or open tenders marketed by tendering companies. We can solicit our customers (including the end customers in respect of our catalogued special-purpose tobacco machinery products) on our own.

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As our products are highly customised, our sales and marketing personnel as well as our technical personnel undertake initial discussions with the potential end customers to understand the project requirements. After taking into consideration the different factors in a potential project, which include but are not limited to project costs, technical requirements, our production capacity and expertise, the general manager of Baoying Renheng will determine whether to pursue such project.

If we decide to pursue a project, we would commence further discussions with the potential customers and submit a proposal for their internal review and consideration or submit a tender to the tendering companies. The proposal and tender documents normally contain our tailor-made technical design for the project as well as our bidding price based on the project requirements. The potential customer or the tendering company would take into account a number of factors, including but not limited to, the project design, bidding price, technical capability and track record of the bidders in their selection process. In all cases, our technical personnel are responsible for the project design based on the specifications and requirements of the potential customers whilst our sales and marketing personnel will negotiate the terms and conditions of the contracts.

(ii) Negotiations on contract terms and signing of contracts

If the potential customer is satisfied with our custom-made technical design for the project, we will enter into a technical agreement with the potential customer, which sets out the detailed technical specifications and requirements of the project, and then proceed to conclude a sales contract with the customer. We agree on the contract terms directly with the customers. Nevertheless, the pricing of our catalogued special-purpose tobacco machinery shall follow the guidance prices set out in the Pricing Guidelines and Pricing Approval 2010. For sales transactions in respect of our catalogued special-purpose tobacco machinery products, namely casing and flavouring systems, PF systems and PP systems, the purchasers are required under the Measures on Administration of Procurement to send a purchase report to the direct reporting unit or competent state administrative bureau or authority for approval. If the relevant tobacco monopoly authority has no objection to the purchase report, they shall send the report to STMA attached with their opinions. The competent authority under STMA which is in charge of fixed asset investment shall issue a purchase approval document on purchasing tobacco machinery regulated by STMA. The purchase report should contain relevant information including, among others, the name of the purchaser, the name of the catalogued special-purpose machinery, the model number, the name of manufacturer, estimated price and other cost relating to the purchase. The contract can be executed only after the purchaser has presented the purchase approval document. Although we do not enter into sales contracts in respect of catalogued special-purpose tobacco machinery with our end customers directly but are required under the relevant PRC regulations to engage CTMC to handle such procurement for the end customer, the negotiation of the underlying contract terms regarding each of our projects, such as the price, technical requirements, delivery method, time and place of delivery, is conducted directly between us and our end customers. CTMC is not involved in the negotiations regarding the procurements of catalogued special-purpose tobacco machinery which are carried out between our Group and the end customers. Except for the entering into of the sale and purchase agreements with us in connection with catalogued special-purpose tobacco machinery procurements made by our end customers, CTMC is not involved in other steps of our project operation process. In respect of non-catalogued ancillary tobacco machinery products, parts, components and/or devices which are not listed in all of the Tobacco Machinery Documents, we may enter into agreement directly with our end customers.

(iii) Formulation of implementation plans

Once a sales contract is signed, our sales and marketing department, technical department, production department as well as procurement department will form a project implementation team to design and formulate a project implementation plan. An expected project timetable setting out, among others, the schedule for technical design documentation, procurement of raw materials, parts and components and production as well as expected delivery date will be set up. Our technical department will then work out the detailed design of the product with reference to the technical specifications and requirements as set out in the technical agreement. The project implementation team will, based on the detailed product design, determine the procurement of the necessary raw materials, parts and components, set out the production sequence for the processing of raw materials, parts and components, allocate the necessary personnel, machinery and equipment as well as procure subcontractors (if necessary) for the implementation of our production sequence. This process normally takes 1 week to 2 months, depending on the size and complexity of the project.

(iv) Procurement of raw materials, parts and components from approved suppliers

Our procurement department procures our raw materials, parts and components based on the project implementation plan taking into account the raw materials, parts and components in stock. We enter into procurement arrangements with our suppliers to secure the necessary raw materials, parts and components required for individual projects after we have entered into sales contracts with our customers in order to ensure the timely delivery of raw materials, parts and components in accordance with the production schedule, and avoid fluctuation in the prices of the raw materials, parts and components during the course of the project. We maintain a list of approved suppliers and procure raw materials, parts and components from such suppliers. In the selection of our approved suppliers, we take into account different factors, including but not limited to, the pricing and quality of the raw materials, parts and components, stability of supply and delivery, the credit period offered by the suppliers as well as their reputation. We generally review the list of approved suppliers on an annual basis.

(v) Inspection and processing of raw materials, parts and components into semi-finished products

The raw materials, parts and components we procured are inspected before our production department processes them into semi-finished parts in accordance with the specifications and requirements set out in the implementation plan of a particular project. The processing generally includes cutting raw materials into required shapes, drilling, bending, welding and machine processing. The semi-finished parts prepared at this stage include metal structural frames, various types of tanks, piping systems as well as working platforms, and are integrated with procured parts and components such as weighing instruments, flow meters, blenders, valves, hydraulic systems, counter modules and electronic devices to form semi-finished products. The semi-finished products are inspected and tested for any defect at our production site before delivery to the cigarette manufacturers or tobacco redrying factories for installation to ensure that they meet the specifications and requirements of the customers. The semi-finished products will undergo painting or sand blasting process at this stage. This process normally takes 1.5 month to 5 months, depending on the size and complexity of the project.

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(vi) Packaging, warehousing and delivery

The semi-finished products as well as procured parts and components are packaged and stored in our warehouse ready to be delivered to the production sites of the cigarette manufacturers or tobacco redrying factories for installation according to the schedule of the customers. Pursuant to relevant PRC regulations, a delivery permit in respect of catalogued special-purpose tobacco machinery products must be obtained from STMA prior to delivery to the cigarette manufacturers or tobacco redrying factories.

(vii) Installation and acceptance at the end customer's site

After the semi-finished products as well as procured parts and components are delivered to the production sites of the cigarette manufacturers or tobacco redrying factories, we will carry out the assembly, installation, tuning and testing of the products as well as assist our customers in the integration of the products into their production line for a trial run to ensure that the products function properly in accordance with the customers' requirements. The duration of the installation and testing process varies from 2.5 weeks to 4 months depending on the size and complexity of the project. Our products are deemed to be accepted by our customers once a certificate of normal operation is signed by the cigarette manufacturers and tobacco redrying factories.

(viii) Maintenance and other services

We generally provide a warranty period of 12 months for our tobacco machinery products and services for no extra charge under the tobacco machinery sales contracts. The warranty period is agreed with the cigarette manufacturers or tobacco redrying factories upon signing of the sales contracts. During the warranty period, we are responsible for any defect in the products and provide maintenance and repair services in respect of defects covered by the warranty. An original acknowledgement of inspection shall be signed by us and the end customer to confirm the final acceptance of the products.

In addition to the maintenance services during the warranty period, we also offer repair and maintenance, overhaul and modification services to cigarette manufacturers and tobacco redrying factories in respect of tobacco machinery products manufactured by us or other tobacco machinery manufacturers. We would enter into a contract directly with our customers in respect of such services. Our fees would vary depending on the scope of services to be provided, the specifications and requirements of the customers as well as the complexity of the project. The service fee for provision of the above services is calculated based on a certain percentage of the costs incurred by our Group in system design, production, integration, management service, installation, software development and transportation as well as insurance costs, taking into account of the market conditions and the business relationship with the relevant customer.

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PRODUCTS AND SERVICES

Our principal business is the manufacture, sale and provision of maintenance, overhaul and modification services in respect of catalogued special-purpose tobacco machinery and related components and devices not listed in all of the Tobacco Machinery Documents from which we derived approximately 92.6%, 95.4% and 93.0% of our turnover for each of the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. We manufacture three types of catalogued special-purpose tobacco machinery, namely casing and flavouring system, PP system and PF system, to meet the needs of cigarette manufacturers and tobacco redrying factories in the PRC.

In addition to our catalogued special-purpose tobacco machinery, we are also engaged in the sale of parts of tobacco machinery products and the manufacture, sale and provision of maintenance, overhaul and modification services in respect of non-catalogued ancillary tobacco machinery products, which mainly include dedusting systems and swelling agent delivery systems.

Our business is project based and all of our tobacco machinery products are custom-made to meet the specifications and requirements of cigarette manufacturers and tobacco redrying factories in the PRC. Therefore, our turnover of catalogued special-purpose tobacco machinery also includes that derived from sales of parts and sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents and not contracted with CTMC but form integral parts of the customised systems. For this type of sales, we may enter into agreement directly with our end customers in order to meet the functional specification of their systems.

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The following table sets forth a breakdown of our turnover by project category during the Track Record Period:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Catalogued special-purpose tobacco machinery projects								
Sales of tobacco machinery and parts/components/devices (<i>Note i</i>)								
Casing and flavouring systems	37,873	52.2	48,097	52.5	16,982	66.5	55,237	85.4
PF systems	10,545	14.5	13,790	15.0	5,215	20.4	936	1.5
PP systems	4,858	6.7	2,381	2.6	–	–	–	–
	<u>53,276</u>	<u>73.4</u>	<u>64,268</u>	<u>70.1</u>	<u>22,197</u>	<u>86.9</u>	<u>56,173</u>	<u>86.9</u>
Provision of maintenance, overhaul and modification services								
Casing and flavouring systems	11,288	15.5	13,091	14.3	769	3.0	2,137	3.3
PF systems	1,854	2.6	4,015	4.4	1,192	4.7	1,540	2.4
PP systems	805	1.1	6,095	6.6	510	2.0	273	0.4
	<u>13,947</u>	<u>19.2</u>	<u>23,201</u>	<u>25.3</u>	<u>2,471</u>	<u>9.7</u>	<u>3,950</u>	<u>6.1</u>
Sub-total								
Casing and flavouring systems	49,161	67.7	61,188	66.8	17,751	69.5	57,374	88.7
PF systems	12,399	17.1	17,805	19.4	6,407	25.1	2,476	3.9
PP systems	5,663	7.8	8,476	9.2	510	2.0	273	0.4
	<u>67,223</u>	<u>92.6</u>	<u>87,469</u>	<u>95.4</u>	<u>24,668</u>	<u>96.6</u>	<u>60,123</u>	<u>93.0</u>
Other projects and products								
Sales of non-catalogued ancillary tobacco machinery (<i>Note ii</i>)								
	1,636	2.2	2,125	2.3	–	–	2,286	3.5
Provision of maintenance, overhaul and modification services								
	3,757	5.2	498	0.5	870	3.4	–	–
Sales of hot stamped foil products								
	–	–	1,621	1.8	–	–	2,242	3.5
	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Sub-total								
	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Total								
	<u><u>72,616</u></u>	<u><u>100.0</u></u>	<u><u>91,713</u></u>	<u><u>100.0</u></u>	<u><u>25,538</u></u>	<u><u>100.0</u></u>	<u><u>64,651</u></u>	<u><u>100.0</u></u>

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- Notes:* (i) Turnover of catalogued special-purpose tobacco machinery projects contracted with CTMC amounted to approximately HK\$53,208,000, HK\$60,589,000 and HK\$21,893,000, representing approximately 73.3%, 66.1% and 33.9% of our total turnover during the Track Record Period. Turnover generated from catalogued special-purpose tobacco machinery projects also includes that derived from sales of parts and sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents but form integral parts of the customised systems and are not contracted with CTMC, which amounted to approximately HK\$68,000, HK\$3,679,000 and HK\$34,280,000, representing 0.1%, 4.0 % and 53.0% of our total turnover respectively during the Track Record Period. Despite the separate sale and purchase agreement, as these components and/or devices were included in the technical specification of the corresponding catalogued special-purpose tobacco machinery projects and cannot function separately from the catalogued special-purpose tobacco machinery system, the revenue derived from the sales of these items is classified under the relevant category of catalogued special-purpose tobacco machinery projects. The significant increase in the sales of these components and/or devices during the six months ended 30 June 2011 was mainly attributable to substantial turnover recognised from the customised casing and flavouring system with movable tanks project with our customer in Kunming during the period. For further details, please refer to the paragraph headed “Description of selected consolidated statement of comprehensive income line items – Turnover” under the “Financial information” section in this prospectus.
- (ii) Non-catalogued ancillary tobacco machinery products mainly comprised dedusting systems and swelling agent delivery systems.

In addition, in late 2010, through our established business relationship with a cigarette manufacturer in the PRC, we identified a new business opportunity in the PRC cigarette packaging industry. On 23 December 2010, we entered into a contract with 遼寧紅塔實業有限公司 (Liaoning Hongta Industrial Co., Ltd.*, “Liaoning Hongta”), which is engaged in the sale of packaging material products and an Independent Third Party, to supply hot stamped foil used in cigarette packaging. We sourced the hot stamped foil from 佛山市三水金鑄包裝材料有限公司 (Foshan Sanshui Jin Lei Packaging Material Co., Ltd.*, “Jin Lei”), a manufacturer of hot stamped foil and an Independent Third Party, which directly delivered the products to our customer in December 2010. During the six months ended 30 June 2011, in addition to Liaoning Hongta, we have also entered into contracts with another customer, which is an Independent Third Party, to supply hot stamped foil used in cigarette packaging. Meanwhile, we have sourced the hot stamped foil from three suppliers, including Jin Lei, which are all Independent Third Parties. To the best of our Directors’ knowledge, each of the customers and suppliers of our hot stamped foil products is a private enterprise. The following summarises the major contractual terms of the sales contract with our customers and the purchase contract with our suppliers of hot stamped foil products:

Typical terms of sales contract with our customers of hot stamped foil products

- **Payment term.** The customer is required to make full payment within 60 days after the issue of invoice.
- **Product delivery.** We are required to deliver the products to the customer’s raw material warehouse or other designated place at our own cost.
- **Quality.** We shall ensure that the hot stamped foil supplied to the customer complies with the quality requirement as agreed between us and the customer in advance.

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- **Breach of contract.** In case of late delivery, we are subject to a penalty of 0.3% of the invoice amount on a daily basis. In case of cancellation of the contract without cause by any contract party, there is a penalty of 30% of the invoice amount payable by the cancelling party.
- **Term.** One to two months.

Typical terms of purchase contract with our suppliers of hot stamped foil products

- **Payment term.** We are required to make full payment before the end of the month during which the invoice is issued.
- **Product delivery.** The supplier shall deliver the products within 15 days upon receipt of order, or any other date as agreed between us at their own cost to our designated place.
- **Quality.** The supplier shall ensure the quality of the hot stamped foil used in cigarette packaging is in compliance with the relevant industry standard in PRC.
- **Warranty period.** We are granted a warranty period of 3 months after the delivery of products by the supplier.
- **Breach of contract.** Any unsolved dispute will be settled in accordance with the PRC Contract Law.
- **Term.** One to two months.

Our Directors confirmed that, during the Track Record Period and up to the Latest Practicable Date, neither our Group nor our customers of hot stamped foil products had breached the terms of the sales contracts.

We sourced the hot stamped foil at the request of the customers according to their specifications including quantity, size, colour and quality. We were able to procure the products required and supplied them to the customers at a competitive price. In addition, we monitored the quality of the products manufactured through contact with the suppliers and arranged delivery in accordance with the customers' schedule. Our pricing policy for the sale of hot stamped foil is on a cost plus basis, depending on the type of hot stamped foil supplied. During the Track Record Period, the relevant margin ranged between 26.3% and 67.9%.

The turnover derived from the sale of hot stamped foil was approximately HK\$1,621,000 and HK\$2,242,000 for the year ended 31 December 2010 and the six months ended 30 June 2011 respectively, representing approximately 1.8% and 3.5% of our turnover for the corresponding year/period. Although our Directors believe that the new hot stamped foil trading business will provide another source of income to our Group, it is not our current intention to establish this trading business as part of our core business. Furthermore, as we procure the hot stamped foil products and supply them to the customers

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without further processing, the hot stamped foil trading business does not require additional skills, machinery or utilisation of our existing production capacity and resources, and thus our Directors are of the view that this new trading business will not likely affect our tobacco machinery business. As at the Latest Practicable Date, the hot stamped foil trading business was only at an infancy stage and we did not have any concrete plan regarding the development of this new business.

Catalogued special-purpose tobacco machinery products

Casing and flavouring systems

The taste and texture of different brands of cigarettes vary depending on the proprietary brand recipes of the cigarette manufacturers. Casings and flavours play an important role in creating the taste and texture of cigarettes. Casings can improve smoke quality and experience by reducing the harshness of tobacco, aiding moisture retention and replacing the sugar lost during the cigarette manufacturing process while flavours are added to the tobacco to give each brand its unique taste characteristics. Our casing and flavouring system is a custom-made automated system designed for the purpose of creating the signature taste of cigarettes by blending numerous kinds of flavours and casings according to the unique recipes of individual cigarette brands. Each cigarette manufacturer has its own specifications and requirements for the casing and flavouring system, varying from the number of tanks, the overall frame structure and the devices equipped with the casing and flavouring system. In general, our casing and flavouring systems can be classified into three types: (i) traditional casing and flavouring system; (ii) casing and flavouring system equipped with storage, retrieval and feeding devices; and (iii) casing and flavouring system with movable tanks.

Traditional casing and flavouring system

Our traditional casing and flavouring system comprises seven major parts including electronic weighing instruments, storage tanks, blending tanks, interconnected piping system, blenders, heaters and a computer system.

Casings and flavours are fed manually into the system's storage tanks which are interconnected by a series of pipelines. The casing and flavouring system is controlled by a computer system which stores the parameters of different cigarette recipes and manages the distribution and blending of numerous kinds of flavours and casings according to the recipes. All storage tanks are equipped with electronic weighing instruments. The casings and flavours are delivered via a pipeline to the blending tanks where the blending of casings and flavours will be carried out. The blending tanks are equipped with electronic weighing instruments, heaters and blenders to measure, heat and blend the casings and flavours. The weights of the blending tanks are monitored by the computer system on a real-time basis. After blending, the processed casing and flavour mixtures are delivered either to the processed mixture storage tanks ready for the spraying process or directly to the spraying device through the piping system. The computer system also provides the cigarette manufacturers with data and information regarding the operation of the casing and flavouring system to facilitate them in managing and utilising their systems more efficiently.

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The following is an image of a traditional casing and flavouring system manufactured by us.



Casing and flavouring system equipped with storage, retrieval and feeding devices

Leveraging on our experience and expertise in casing and flavouring systems, we have designed a casing and flavouring system that can be equipped with mechanical devices in the storage, retrieval and feeding of semi-processed flavour and casing mixtures for the blending process. These devices are controlled by a computer system which limits the chance of human error in the process. A mechanical device is deployed to manage the receipt, storage and movement of the semi-processed casing and flavour mixtures within the warehouse and the site of the casing and flavouring system utilising a barcode system with the relevant information being stored in a central database. Once the computer system sends out the signal for collecting the semi-processed mixtures, the mechanical device would automatically identify and retrieve the required containers and transport them to the site of the casing and flavouring system where a mechanical arm will lift the containers and automatically feed the semi-processed flavour and casing mixtures into the storage tanks for further processing.

In May 2010, we secured a contract to supply a custom-made casing and flavouring system with storage, retrieval and feeding devices for a cigarette manufacturer in Shanghai. The installation and testing of this system have been completed in December 2010. We will continue to provide assistance to the customer after the installation process to ensure that our product works properly to its satisfaction.

Casing and flavouring system with movable tanks

With our strong development and customisation capabilities, we developed a casing and flavouring system with movable tanks in 2010. With the traditional casing and flavouring system, the tanks are interconnected by a series of pipelines and the ingredients are delivered from the storage tanks via a single pipeline to the blending tank. The tanks under the new system are not interconnected. The raw materials are stored in individual tanks managed by a bar code system. Individual ingredients

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are fed directly into the movable tanks transported on a conveyor belt to the blender. As in the traditional casing and flavouring system, this new system is also controlled by a computer system which stores the parameters of different cigarette recipes and manages the distribution and blending of numerous kinds of flavours and casings according to the recipes. The semi-processed casing and flavour mixtures in the movable tanks are then stored in containers ready for further processing by the cigarette manufacturers.

We believe that with the cigarette brand consolidation in the PRC tobacco industry, domestic cigarette manufacturing groups would aim to standardise the taste and texture of individual cigarette brands and begin to centralise the processing of casings and flavours. Our new casing and flavouring system will cater to the needs of the cigarette manufacturing groups. The semi-processed casing and flavouring mixtures are prepared at the central blending centre of a cigarette manufacturing group without solvents and are therefore highly concentrated. The cigarette manufacturing group will incur raw material loss during the pipeline delivery of the flavour and casing mixtures to the blending tank if the traditional casing and flavouring systems are used. Our new system will solve this problem as individual ingredients are fed directly to movable tanks which will be transported on a conveyor belt to the blender. The semi-processed casing and flavour mixtures in the movable tanks are stored in containers ready for distribution to the local production sites of the cigarette manufacturing groups.

In April 2010, we contracted with CTMC to supply a customised casing and flavouring system with movable tanks to a cigarette manufacturer in Kunming. We also contracted directly with this cigarette manufacturer to supply other components and devices which are not listed in all of the Tobacco Machinery Documents but form integral part of this customised system. As the first of its kind system built by our Group, more new components and devices, as compared with those comprised in the traditional casing and flavouring system, have to be equipped with the system so that it could function in accordance with the design as required and agreed with the end customer. The customisation of the said casing and flavouring system required the installation of certain components and devices which are not listed in all of the Tobacco Machinery Documents to meet our customer's specifications. Due to the larger scale, more customisation requests and higher degree of complexity of the customised system, the contract value for our supply of these components and devices accounted for a significant portion of the project's aggregate contract value, thus leading to a high turnover attributable to the sales of parts and sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents during the six months ended 30 June 2011. The part of this project contracted with CTMC was completed and the respective certificate of normal operation was obtained from the cigarette manufacturer in May 2011, while the remaining part of this project is expected to be completed in November 2011.

To meet the needs of different cigarette manufacturers, we can incorporate a spraying device to our casing and flavouring systems. A spraying device is designed to spray the processed casing and flavour mixtures onto the cut tobacco during the cigarette production process. After blending, the processed casing and flavour mixtures are delivered either to the processed mixture storage tanks ready for the spraying process or directly to the spraying device through the piping system. The spraying device comprises three major parts, namely the spraying nozzle, the metal cylinder and storage tanks. The spraying process is controlled by a computer programme.

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The table below sets forth our casing and flavouring system contracts with contract value above RMB5 million completed during the Track Record Period, which in aggregate accounted for approximately 61.8%, 73.6% and 81.9% of the total contract value for our completed casing and flavouring system contracts during the Track Record Period respectively:

Name/type of contract party	Location of project	Contract date	Completion date	Aggregate contract value (RMB'000)	Description
CTMC	Kunming, Yunnan	19 April 2010	31 May 2011 <i>Note i</i>	29,423 <i>Note ii</i>	Supplying 1 set of casing and flavouring system <i>Note iii</i>
CTMC	Guizhou	13 November 2009	24 December 2010 <i>Note i</i>	17,177 <i>Note ii</i>	Supplying 2 sets of casing and flavouring systems <i>Note iii</i>
CTMC	Fujian	9 March 2009	15 December 2010 <i>Note i</i>	13,000 <i>Note ii</i>	Supplying 1 set of casing and flavouring system <i>Note iii</i>
CTMC	Shanghai	18 May 2010	1 December 2010	9,990 <i>Note ii</i>	Supplying 1 set of casing and flavouring system and spraying device <i>Note iii</i>
CTMC	Fujian	9 December 2008	9 October 2009 <i>Note i</i>	9,880 <i>Note ii</i>	Supplying 1 set of casing and flavouring system <i>Note iii</i>
CTMC	Shandong	9 December 2008	15 August 2009	9,300 <i>Note ii</i>	Supplying 1 set of casing and flavouring system <i>Note iii</i>
CTMC	Tianjin	23 December 2008	21 December 2009 <i>Note i</i>	6,650 <i>Note ii</i>	Supplying 1 set of casing and flavouring system
A cigarette manufacturer	Yunnan	10 December 2009	3 October 2010 <i>Note i</i>	5,550	Modifying storage tanks and piping system

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Notes:

- (i) The time needed for completing our projects may vary from 1 month to 9 months depending on the size of our projects. More than 9 months were required to complete this project due to the postponement in the delivery/ installation schedule requested by our customer/end customer.
- (ii) The aggregate contract value of the contract entered into with CTMC included that for the supply of non-catalogued components and/or devices.
- (iii) In addition to the contract listed, our Group also entered into supplemental sale and purchase agreement directly with the end customer in respect of supply of components and/or devices which were not listed in all of the Tobacco Machinery Documents but form integral parts of the customised system under the same project.

PF system

Our PF system is a pneumatic-based equipment used in the cigarette production process to deliver the processed cut tobacco inside an enclosed piping system to the cigarette wrapping machine through which the processed cut tobacco are wrapped around by cigarette papers and then sealed to form continuous rods. The continuous rods are then cut to proper length and sealed with filters for packing. The advantages of our PF system are that pneumatic delivery can reduce the possible damage to the structure of the processed cut tobacco and shorten the delivery time of the processed cut tobacco to the cigarette wrapping machine as compared with mechanical delivery through conveyor system. Our PF system can be installed with two to eight pipes with delivery capacity of up to 750 kilograms of processed cut tobacco per hour for each tube depending on the requirements of the cigarette manufacturers.

The following is an image of a PF system manufactured by us.



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The table below sets forth our PF system contracts with contract value above RMB1 million completed during the Track Record Period, which in aggregate accounted for approximately 51.4%, 76.9% and 43.1% of the total contract value for our completed PF system contracts during the Track Record Period respectively:

Name/type of contract party	Location of project	Contract date	Completion date	Aggregate contract value (RMB'000)	Description
CTMC	Guizhou	17 March 2010	21 June 2010	3,496 ^{Note ii}	Supplying 8 sets of PF systems
CTMC	Yunnan	13 July 2009	26 August 2010 ^{Note i}	2,760	Supplying 6 sets of PF systems
CTMC	Shandong	1 December 2008	6 March 2009	2,622 ^{Note ii}	Supplying 6 sets of PF systems
CTMC	Yunnan	29 July 2009	7 September 2009	1,840 ^{Note ii}	Supplying 4 sets of PF systems
CTMC	Chongqing	22 January 2010	3 April 2010	1,840 ^{Note ii}	Supplying 4 sets of PF systems ^{Note iii}
A tobacco machinery manufacturer	Tianjin	15 April 2009	1 April 2010 ^{Note i}	1,732	Supplying parts for 6 sets of PF systems
CTMC	Sichuan	31 May 2010	1 December 2010	1,660 ^{Note ii}	Supplying 4 sets of PF systems ^{Note iii}
CTMC	Yunnan	23 December 2008	7 September 2009	1,380 ^{Note ii}	Supplying 3 sets of PF systems
A cigarette manufacturer	Sichuan	28 June 2010	8 December 2010	1,280	Modifying PF systems
A cigarette manufacturer	Yunnan	20 January 2009	2 April 2009	1,250	Providing maintenance for PF systems
CTMC	Sichuan	28 October 2009	30 October 2010 ^{Note i}	1,110 ^{Note ii}	Supplying 3 sets of PF systems ^{Note iii}
A cigarette manufacturer	Henan	7 January 2011	5 May 2011	1,048	Modifying PF systems

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Notes:

- (i) The time needed for completing our projects may vary from 1 month to 9 months depending on the size of our projects. More than 9 months were required to complete this project due to the postponement in the delivery/ installation schedule requested by our customer/end customer.
- (ii) The aggregate contract value of the contract entered into with CTMC included that for the supply of non-catalogued components and/or devices.
- (iii) In addition to the contract listed, our Group also entered into supplemental sale and purchase agreement directly with the end customer in respect of supply of components and/or devices which were not listed in all of the Tobacco Machinery Documents but form integral parts of the customised system under the same project.

PP system

Our PP system is a mechanical system designed for use by tobacco redrying factories for the compressing and packing of tobacco leaves into cartons to facilitate delivery to the cigarette manufacturers for further processing. The system comprises principally a series of conveyor belts, a vertical steel container, a compressor and a sealing machine. The tobacco leaves are transported on the conveyor belts to the top end compartment of the vertical steel container of the PP system. After the compartment is filled up, the tobacco leaves will be released and fed through the vertical container into a carton placed at the bottom of the container. The compressor will compress the tobacco leaves in the carton twice. The carton will then be transported on a conveyor belt to the sealing machine for sealing. The production capacity of our PP system is estimated to be approximately 12,000 kilograms of tobacco leaves per hour or 50 cartons per hour.

The following is an image of a PP system manufactured by us.



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The table below sets forth our PP system contracts with contract value above RMB1 million completed during the Track Record Period, which in aggregate accounted for approximately 85.8%, 79.1% and nil of the total contract value for our completed PP system contracts during the Track Record Period respectively:

Name/type of contract party	Location of project	Contract date	Completion date	Aggregate contract value (RMB'000)	Description
CTMC	Yunnan	29 July 2009	18 September 2009	2,891	Supplying 3 sets of PP systems ^{Note ii}
CTMC	Henan	15 September 2009	3 December 2010 ^{Note i}	2,410	Supplying 3 sets of PP systems ^{Note iii}
CTMC	Hunan	8 June 2009	19 October 2009	2,120	Supplying 1 set of PP system
A tobacco redrying factory	Yunnan	15 October 2009	27 November 2010 ^{Note i}	1,706	Supplying parts and providing installation services of PP systems ^{Note ii}
A tobacco redrying factory	Henan	8 November 2009	3 December 2010 ^{Note i}	1,579	Supplying parts and providing installation services of PP systems ^{Note iii}
A tobacco redrying factory	Yunnan	4 August 2010	1 December 2010	1,110	Providing maintenance for PP system

Notes:

- (i) The time needed for completing our projects may vary from 1 month to 9 months depending on the size of our projects. More than 9 months were required to complete this project due to the postponement in the delivery/installation schedule requested by our customer/end customer.
- (ii) These contracts were separately entered into with CTMC and the end customer for the same PP system project.
- (iii) These contracts were separately entered into with CTMC and the end customer for the same PP system project.

Non catalogued ancillary tobacco machinery products

Non catalogued ancillary tobacco machinery products manufactured by us mainly include dedusting systems and swelling agent delivery systems.

Dedusting system

We offer two types of dedusting systems that can be equipped with different machinery in the cigarette production line.

A typical dedusting system is equipped with the cigarette wrapping machine and is designed to extract dust and broken cut tobacco produced during the cigarette wrapping process by a vacuum and delivered to a dust removal device through the pipeline system.

To meet the needs of cigarette manufacturers, we have developed another type of dedusting system with enhanced air stabilisation capabilities. This dedusting system is equipped with the PF system to remove dust and unused cut tobacco from the enclosed piping system connected between the PF system and the cigarette wrapping machine during the pneumatic feeding process. In addition, this type of air stabilisation dedusting system can be applied to stabilise the air flow velocity by adjusting certain valves in the enclosed piping system in order to reduce the damage to cut tobacco as well as to enhance the processing efficiency of the cigarette wrapping machine. The air stabilisation dedusting system is also installed with an air flow velocity detecting device and an automatic air flow adjusting device to reduce the breakage of tobacco and the blockage created by cut tobacco, resulting in better control of the density of processed cut tobacco in each cigarette during the wrapping process to maintain the quality of the cigarettes.

The following is an image of a dedusting system manufactured by us.



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Swelling agent delivery system

Swelling agent, a chemical substance used in the filter production process, is manually fed to the filter rod forming machine at the factories of the cigarette manufacturers. Our swelling agent delivery system is designed for the automatic supply of the swelling agents to the filter rod forming machine during the cigarette production process.

The table below sets forth our dedusting system and swelling agent delivery system contracts with contract value above RMB1 million completed during the Track Record Period, which in aggregate accounted for approximately 22.3%, 29.3% and 30.4% of the total contract value for our completed contracts for other projects during the Track Record Period respectively:

Type of contract party	Location of project	Contract date	Completion date	Aggregate contract value (RMB'000)	Description
A cigarette manufacturer	Zhejiang	9 July 2010	10 May 2011 <i>Note</i>	1,344	Supplying 1 set of swelling agent delivery system
A cigarette manufacturer	Tianjin	11 November 2008	15 September 2010 <i>Note</i>	1,260	Supplying 1 set of swelling agent delivery system
A cigarette manufacturer	Guizhou	23 January 2009	22 May 2009	1,240	Supplying 1 set of dedusting system

Note: The time needed for completing our projects may vary from 1 month to 9 months depending on the size of our projects. More than 9 months were required to complete this project due to the postponement in the delivery/installation schedule requested by our customer.

Postponement in delivery/installation schedule requested by our customers/end customers

During the Track Record Period, 26, 29 and 8 contracts for which revenue had been recognised, representing approximately 67.2%, 80.4% and 92.8% of our turnover respectively, have experienced postponement in delivery/installation schedule requested by our customers/end customers for periods ranging from approximately 1 month to 10 months. In respect of contracts signed but not completed as at 31 August 2011, we have experienced postponement in delivery/ installation schedule requested by customers for periods up to 22 months. For further information of these contracts, please refer to the sub-paragraph headed "Contracts signed but not completed as at 31 August 2011" below in this section. We believe that it is a usual practice to specify the delivery date in the contracts entered into with our customers. Notwithstanding the above, the delivery date may not be specified in the sale and purchase agreement in cases where the customers cannot confirm the delivery schedule upon entering into the contracts under different circumstances, for instance, (i) the customers are uncertain of the completion time of required preparation work at their premises before machinery installation; and (ii) in cases of provision of services, we can only carry out our work upon instruction of the customers

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after they have temporarily suspended the relevant parts of the production line, the time of which cannot be confirmed by the customers at the time of signing the contract. Therefore, during the Track Record Period, in negotiating the contract terms with our customers, the delivery date of our tobacco machinery products may not be specified in the contract or may be subject to customers' further delivery instructions. In cases where the delivery date is not specified or is subject to customer's instruction pursuant to the terms in the sale and purchase agreement, we are not entitled to any compensation from the customers for the postponement in delivery/installation schedule requested by them. In other cases where the delivery date is specified in the sale and purchase agreement, despite the fact that we are entitled to compensation from the customer for postponement under relevant PRC laws, we in general will still accommodate the customer's request to defer product delivery/installation to meet their operation needs.

The following sets out the aggregate contract value of contracts from which we have derived revenue during the Track Record Period, where the delivery date was not specified.

	For the year ended 31 December				For the six months ended 30 June	
	2009		2010		2011	
	Number of contracts	Aggregate contract value (RMB'000)	Number of contracts	Aggregate contract value (RMB'000)	Number of contracts	Aggregate contract value (RMB'000)
Delivery date not specified in the contract	6	2,756	7	3,980	6	653

Our Directors are of the view that our revenue attributable to the above contracts was not material during the Track Record Period. For information about the impact of such postponements on our working capital position, please refer to the risk factor headed "Postponement in delivery/installation schedule requested by our customers/end customers" in the section headed "Risk factors" in this prospectus. Nevertheless, the management as well as the marketing and technical personnel of Baoying Renheng are responsible for monitoring the progress of our projects. In case of any material variation in delivery schedule/installation schedule as previously agreed with customers, we will revise our project implementation plan with respect to the schedule of procurement of raw materials, parts and components as well as our production schedule in order to lessen the impact of such postponements on our working capital position. Despite the fact that our Group did not have any borrowings, mortgages or charges, or material contingent liabilities outstanding as at 31 December 2009 and 2010 and 30 June 2011, and we had bank balances and cash of approximately HK\$5,629,000, HK\$54,383,000 and HK\$40,012,000 as at 31 December 2009 and 2010 and 30 June 2011 respectively, any delay in postponement in delivery/installation schedule of a project, where the amount of payment upon delivery/completion of installation is financially significant, may materially and adversely affect our working capital position.

Going forward, our Group intends to specify the delivery date in all of our sale contracts entered into with our customers in the future. In the event that the original delivery date cannot be met by the customers, we will allow the postponement request from our customers within a period

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of six months from the original delivery date, during which we will continue to follow up with the customer in confirming a new delivery date. After such period, we will request the customer to sign a supplemental contract with us to reconfirm the delivery date within six months from the date of such contract. Thereafter, if the customer cannot accept our product delivery by the agreed delivery date or within 12 months of the original delivery date, we will terminate the sale contract and will claim on the customer for all costs incurred in excess of the deposit received from this customer in respect of the contract.

Contracts signed but not completed as at 31 August 2011

The aggregate value of contracts signed with our customers as of 31 August 2011 less revenues recognised in connection with such contracts up to and including the same date amounted to approximately RMB134,788,000. Among them, 16, 9, 5 and 4 contracts relate to casing and flavouring system, PF system, PP system and other projects respectively. Subject to the delivery and final acceptance of our products and services by the end customers, we expect that these projects will be completed by December 2012.

The table below sets forth our contracts on hand in relation to casing and flavouring system projects with contract value above RMB5 million, and in relation to PF system and PP system projects and other projects with contract value above RMB1 million as of 31 August 2011:

Casing and flavouring system projects

Name/type of contract party	Location of project	Contract date	Aggregate contract value (RMB'000)	Description
A cigarette manufacturer	Kunming, Yunnan	22 April 2010	49,815 <i>Note i</i>	Supplying components and devices of casing and flavouring systems
CTMC	Hunan	19 April 2011	22,274	Supplying 1 set of casing and flavouring systems
CTMC	Guangxi	29 March 2011	17,435	Supplying 1 set of casing and flavouring systems
CTMC	Chongqing	2 August 2010 <i>Note ii</i>	10,935	Supplying 1 set of casing and flavouring systems
CTMC	Guizhou	13 November 2009 <i>Note iii</i>	7,792	Supplying 2 sets of casing and flavouring systems
A cigarette manufacturer	Kunming, Yunnan	13 January 2011	6,780	Supplying components and devices

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- Notes:* (i) Revenue recognised in respect of this project amounted to approximately HK\$30,638,000 up until 31 August 2011. Other than this project, no revenue has been recognised in respect of all other casing and flavouring system projects, PF system projects, PP system projects and other projects listed herein.
- (ii) The time needed for completing this project exceeded 9 months due to the postponement in the delivery/ installation schedule requested by our end customer in September 2010. No revenue was recognised in respect of this project during the Track Record Period and up until the Latest Practicable Date as the casing and flavouring system was still pending delivery instruction from the end customer and thus the first stage of completion had not been fulfilled. We accepted the postponement request from this end customer based on mutual agreement in order to maintain business relationship with this end customer. The costs incurred for this casing and flavouring system project during the Track Record Period and up until the Latest Practicable Date amounted to approximately HK\$2,845,000. Based on on-going communication with this end customer, our Directors are of the view that the incurred costs can be recovered and we expect this project will be completed by December 2012. In addition to this project, our Group also has 1 other contract on hand with this end customer with contract value of approximately RMB1,720,000.
- (iii) The time needed for completing this project exceeded 9 months due to the postponement in the delivery/ installation schedule requested by our customer in December 2009. No revenue was recognised in respect of this project during the Track Record Period and up until the Latest Practicable Date as the casing and flavouring system was still pending delivery instruction from the end customer and thus the first stage of completion had not been fulfilled. We accepted the postponement request from this end customer based on mutual agreement in order to maintain business relationship with this end customer. The costs incurred for this casing and flavouring system project during the Track Record Period and up until the Latest Practicable Date amounted to approximately HK\$4,717,000. Based on on-going communication with this end customer, our Directors are of the view that the incurred costs can be recovered and we expect this project will be completed by December 2012. In addition to this project, our Group also has 3 other contracts on hand with this end customer with aggregate contract value of approximately RMB8,255,000.

PF system projects

Name/type of contract party	Location of project	Contract date	Aggregate contract value (RMB'000)	Description
CTMC	Shanghai	21 December 2009	5,180	Supplying 14 sets of PF system
CTMC	Yunnan	25 March 2010	2,760	Supplying 6 sets of PF system
CTMC	Jiangxi	4 August 2011	2,300	Supplying 5 sets of PF system
CTMC	Guizhou	17 March 2010	1,840	Supplying 4 sets of PF system
A cigarette manufacturer	Chongqing	17 May 2011	1,720	Modifying PF system

BUSINESS

PP system projects

Name/type of contract party	Location of project	Contract date	Aggregate contract value (RMB'000)	Description
CTMC	Yunnan	7 April 2011	2,891	Supplying 3 sets of PP systems ^{Note iv}
A tobacco redrying factory	Yunnan	12 May 2011	1,704	Supplying parts of PP systems ^{Note iv}
A tobacco redrying factory	Henan	21 December 2010	1,380	Supplying parts of PP system

Note: (iv) These contracts were separately entered into with CTMC and the end customer for the same PP system project.

Other projects

Name/type of contract party	Location of project	Contract date	Aggregate contract value (RMB'000)	Description
A cigarette manufacturer	Guizhou	30 September 2010	7,150	Supplying 6 sets of dedusting system
A cigarette manufacturer	Henan	21 February 2011	2,498	Modifying dedusting system

SALES AND MARKETING

We provide our tobacco machinery products and services on a project basis and secure most of our projects through our sales and marketing team which pays regular visits to domestic cigarette manufacturers and tobacco redrying factories. We identify potential projects through business discussions with domestic cigarette manufacturers as well as tobacco redrying factories and through open tenders marketed by tendering companies. During the Track Record Period, sales derived from contracts secured by means of tender accounted for approximately 31.7%, 34.5% and 3.5% of our turnover respectively.

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Our sales and marketing department, consisting of 12 employees as at 31 August 2011, is currently responsible for marketing and promoting to the potential end customers situated in 21 provinces, 4 centrally administered municipalities and 4 autonomous regions across China. Our sales and marketing personnel interact closely with the cigarette manufacturers and tobacco redrying factories to strengthen customer relationships and to identify business opportunities. During their regular visits with the cigarette manufacturers and tobacco redrying factories, our on-the-ground sales and marketing team, consisting of 9 sales managers as at 31 August 2011, would (i) introduce our latest product development information to the cigarette manufacturers and tobacco redrying factories; (ii) gather market information; and (iii) provide prompt feedback to the demands of the cigarette manufacturers and tobacco redrying factories. Each sales manager is responsible for the sales and marketing activities in the regions assigned to him by the Group. In addition, we attend industry meetings through which we are able to better understand the latest developments in the tobacco machinery industry and the tobacco industry in the PRC. We have implemented an incentive scheme for our sales and marketing staff, details of which are set out in the sub-paragraph headed “Selling and distribution costs” under the paragraph headed “Description of selected consolidated statement of comprehensive income line items” in the section headed “Financial information” in this prospectus. The map below shows the regions covered by our sales and marketing team as at the Latest Practicable Date.



Note: The shaded regions in the above map denote the provinces, centrally administered municipalities and autonomous regions covered by our sales and marketing team as at the Latest Practicable Date.

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CUSTOMERS

The end customers of our products and services are generally domestic cigarette manufacturers and tobacco redrying factories in the PRC. In providing our catalogued special-purpose tobacco machinery products as listed in all of the Tobacco Machinery Documents, we enter into contracts directly with CTMC. Furthermore, in order to meet the functional specification of our end customers, we may also contract with end customers directly to supply components and/or devices which are not listed on all of the Tobacco Machinery Documents but form integral parts of the customised systems.

Pursuant to the Measures on Administration of Procurement promulgated by STMA in 2004, CTMC monitors and oversees all domestic catalogued special-purpose tobacco machinery procurement matters between the tobacco machinery manufacturers and the cigarette manufacturers. CTMC acts as an agency to fulfill the relevant regulatory requirements in the procurement arrangements and is not involved in the negotiations regarding the transactions which are carried out between the tobacco machinery manufacturers and the purchasers. Whilst we directly deal with the cigarette manufacturers on the product specifications and final pricing, it is CTMC which enters into agreements with us to procure the machinery products with the instructions to deliver such products to the designated cigarette manufacturers. Notwithstanding the aforesaid regulations, in order to meet the functional specification of our end customers, our custom-made systems may also be equipped with components and/or devices which are not listed in all of the Tobacco Machinery Documents but form integral parts of the customised systems. In such cases, our end customers may enter into a separate sale and purchase agreement with us for such components and/or devices, which is supplemental to the sale and purchase agreement entered into between our Group and CTMC.

In order to ensure that all sales of catalogued special-purpose tobacco machinery are contracted with CTMC as required by relevant regulatory requirements, our Group has adopted the following procedures:

- (i) The technical personnel in charge of our tobacco machinery projects would scrutinise the detailed list of sales order, machinery specification and technical agreement and check the ordered items against all of the Tobacco Machinery Documents to identify those classified as catalogued special-purpose tobacco machinery. The project in-charge would ensure that sale and purchase agreements in respect of all items classified as catalogued special-purpose tobacco machinery are entered into with CTMC; and
- (ii) In respect of sale orders of items which are not classified as catalogued special-purpose tobacco machinery, before signing the relevant technical agreement and sale and purchase agreements with our end customers, the head of our technical department and the general manager of Baoying Renheng will review the details of the purchase and ensure that no item of catalogued special-purpose tobacco machinery is included.

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In respect of control from the supervising government authority, STMA can conduct inspection visits to our Group at their discretion to ascertain whether our Group is in compliance with relevant laws, rules and regulations in relation to the production and sale of catalogued special-purpose tobacco machinery products. Meanwhile, for our end customers, approval from STMA is required before they can contract with CTMC for the procurement of catalogued special-purpose tobacco machinery products.

By virtue of our contractual relationship with CTMC under the aforesaid regulations in respect of catalogued special-purpose tobacco machinery procurement arrangements, CTMC was our largest customer during the two years ended 31 December 2010 and the second largest customer for the six months ended 30 June 2011 and accounted for approximately 73.3%, 66.1% and 33.9% of our turnover for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. Nevertheless, the end customers of our catalogued special-purpose tobacco machinery are generally cigarette manufacturers (in the case of our casing and flavouring systems and PF systems) and tobacco redrying factories (in the case of our PP systems).

For the sale of parts and the provision of the maintenance, overhaul and modification services in respect of our catalogued special-purpose tobacco machinery products, we enter into services contracts directly with the cigarette manufacturers and tobacco redrying factories.

We are also engaged in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of non-catalogued ancillary tobacco machinery products and services, which mainly include dedusting systems and swelling agent delivery systems. In providing such products and services, we enter into contracts directly with the cigarette manufacturers.

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The following sets out the breakdown of our turnover by customer group during the Track Record Period.

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	<i>HK\$'000</i>	%	<i>HK\$'000</i>	%	<i>HK\$'000</i>	%	<i>HK\$'000</i>	%
Catalogued special-purpose tobacco machinery projects								
Casing and flavouring systems								
Sales of tobacco machinery to CTMC	37,805	52.1	46,129	50.3	16,982	66.5	20,957	32.4
Sales of tobacco machinery to other customers	68	0.1	1,968	2.2	-	-	34,280	53.0
Provision of maintenance, overhaul and modification services to other customers	11,288	15.5	13,091	14.3	769	3.0	2,137	3.3
	<u>49,161</u>	<u>67.7</u>	<u>61,188</u>	<u>66.8</u>	<u>17,751</u>	<u>69.5</u>	<u>57,374</u>	<u>88.7</u>
PF systems								
Sales of tobacco machinery to CTMC	10,545	14.5	12,079	13.2	5,215	20.4	936	1.5
Sales of tobacco machinery to other customers	-	-	1,711	1.8	-	-	-	-
Provision of maintenance, overhaul and modification services to other customers	1,854	2.6	4,015	4.4	1,192	4.7	1,540	2.4
	<u>12,399</u>	<u>17.1</u>	<u>17,805</u>	<u>19.4</u>	<u>6,407</u>	<u>25.1</u>	<u>2,476</u>	<u>3.9</u>
PP systems								
Sales of tobacco machinery to CTMC	4,858	6.7	2,381	2.6	-	-	-	-
Sales of tobacco machinery to other customers	-	-	-	-	-	-	-	-
Provision of maintenance, overhaul and modification services to other customers	805	1.1	6,095	6.6	510	2.0	273	0.4
	<u>5,663</u>	<u>7.8</u>	<u>8,476</u>	<u>9.2</u>	<u>510</u>	<u>2.0</u>	<u>273</u>	<u>0.4</u>
Sub-total	<u>67,223</u>	<u>92.6</u>	<u>87,469</u>	<u>95.4</u>	<u>24,668</u>	<u>96.6</u>	<u>60,123</u>	<u>93.0</u>
Other projects and products								
Sales of tobacco machinery to other customers	1,636	2.2	2,125	2.3	-	-	2,286	3.5
Provision of maintenance, overhaul and modification services to other customers	3,757	5.2	498	0.5	870	3.4	-	-
Sales of hot stamped foil products	-	-	1,621	1.8	-	-	2,242	3.5
Sub-total	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Total	<u><u>72,616</u></u>	<u><u>100.0</u></u>	<u><u>91,713</u></u>	<u><u>100.0</u></u>	<u><u>25,538</u></u>	<u><u>100.0</u></u>	<u><u>64,651</u></u>	<u><u>100.0</u></u>

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Our Group had 19, 21 and 12 individual end customers respectively during the Track Record Period. Some of our end customers purchased more than one product category, including catalogued special-purpose tobacco machinery products and/or non-catalogued ancillary tobacco machinery products, from us within the corresponding year/period. The following sets out the number of end customers for each project category during the Track Record Period.

	Year ended 31 December		Six months ended
	2009	2010	30 June 2011
Catalogued special-purpose tobacco machinery projects			
Casing and flavouring systems	12	11	6
PF systems	10	9	5
PP systems	3	7	1
Other projects/products			
Non-catalogued ancillary tobacco machinery projects	6	3	2
Hot stamped foil	–	1	2

The following is an analysis of percentage of sales to our single largest customer and end customer, as well as to our five largest customers and end customers.

	Year ended 31 December		Six months ended 30 June
	2009	2010	2011
% of turnover attributable to	%	%	%
Largest customer	73.3	66.1	47.3 <i>(note)</i>
Largest end customer	21.0	24.8	79.7 <i>(note)</i>
Five largest customers	90.8	81.8	93.0
Five largest end customers	65.2	72.3	93.6

Year of business relationship maintained with our Group during the Track Record Period

Five largest customers	5 months to 10 years
Five largest end customers	1.5 months to 9 years

Note: Our largest customer for the six months ended 30 June 2011, a cigarette manufacturer, was also our largest end customer for the same period. Of our 79.7% turnover derived from this customer, approximately 47.3% was related to sale and purchase agreements entered into directly with this customer, while the remaining 32.4% was related to sale and purchase agreement entered into with CTMC.

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CTMC was our largest customer during the two years ended 31 December 2010, while our largest customer for the six months ended 30 June 2011 was a cigarette manufacturer based in Kunming, Yunnan, the PRC, which sells its products in multiple brands and is ranked among the Top 500 Enterprises of China (中國企業500強) and China's Top 500 Manufacturing Companies (中國製造業500強) in 2011. Turnover derived from our largest customer for the six months ended 30 June 2011 mainly comprised the substantial turnover recognised from the customised casing and flavouring system with movable tanks project with this customer during the period. As the first of its kind system built by our Group, which was of larger scale and higher degree of complexity, the customisation of the said casing and flavouring system required the installation of certain components and devices sourced at higher costs to meet our customer's specifications. As these components and devices were not included in the Tobacco Machinery Documents, their sales were not required to be contracted with CTMC. We contracted directly with this customer, thus leading to a high turnover attributable to this customer and relatively lower turnover attributable to CTMC during the period.

None of our Directors or any of their respective associates or any Shareholders (who or which, to the knowledge of our Directors, held 5% or more of the issued share capital of the Company as at the Latest Practicable Date) had any interest in any of our five largest customers during the Track Record Period.

We did not experience any warranty claims or goods returned during the Track Record Period.

PRICING POLICIES AND CREDIT MANAGEMENT

Pricing policies

The pricing of our casing and flavouring system, PF system and PP system, being catalogued special-purpose tobacco machinery listed on the Tobacco Machinery List, shall follow the State's guidance prices set out in the Pricing Guidelines which were issued by STMA on 30 October 2003 and took effect on 1 January 2004 and the Pricing Approval 2010 which became effective on 23 April 2010 and is supplemental to the Pricing Guidelines. The Pricing Guidelines list the guidance prices for different models of catalogued special-purpose tobacco machinery products, whereas the Pricing Approval 2010 sets out the guidance prices of various casing and flavouring systems which are not specified in the Pricing Guidelines. Subject to negotiations between the tobacco machinery manufacturers and the purchasers, the sales prices may be set within 5% of the guidance prices as stipulated in the Pricing Guidelines. With regard to models of catalogued special-purpose tobacco machinery products not specified by the Pricing Guidelines or the Pricing Approval 2010, the tobacco machinery manufacturers have to file an application to STMA for the pricing approval in relation thereto.

In the event that the guidance price of a catalogued special-purpose tobacco machinery product specified in the Pricing Guidelines or the Pricing Approval 2010 proves to be commercially unacceptable for the tobacco machinery manufacturers to follow, the relevant tobacco machinery manufacturers can make an application to STMA requesting for a revision of the guidance price. Applications for the revision of the guidance prices as specified in the Pricing Guidelines or the Pricing Approval 2010

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can be made to 國家煙草專賣局發展計劃司 (the development and planning division of STMA) and CTMC. However, as at the Latest Practicable Date, no regulations or guidelines had been issued by STMA on the revision of the guidance prices for tobacco machinery. During the Track Record Period and up to the Latest Practicable Date, we did not file any application for the revision of the guidance price and had not received any notice in respect of the revision of the guidance prices as specified in the Pricing Guidelines or the Pricing Approval 2010.

Except for the sales of our catalogued special-purpose tobacco machinery products for which we are required to follow the Pricing Guidelines and the Pricing Approval 2010 in setting our sales prices, we can determine the pricing of our products and services with reference to a number of factors including the types and complexity of the products and services provided, the specifications and requirements of the customers, project costs and the prices set by competitors, subject to arm's length negotiations between our Group and the customers.

Credit and payment terms

We usually grant a credit term of 90 days to our customers, depending on the type of products and services.

Generally, for our sales of casing and flavouring systems, PF systems and PP systems, we receive an initial payment of 20% of the contract value after signing the sales contracts, 70% of the contract value upon delivery of our products, and the remaining 10%, representing warranty retention money, after submission of the original acknowledgement of inspection. CTMC normally makes payments to us by telegraphic transfer.

As regards our non-catalogued ancillary tobacco machinery products and the provision of maintenance, overhaul and modification services, we generally receive an initial payment ranging from 10% to 30% of the contract value upon signing the contracts, and another payment of up to 90% of the contract value upon completion of the product installation and testing or completion of the services. For sales and services contracts without initial payment, we generally receive a payment of up to 90% of the contract value upon completion of the product installation and testing or completion of the services. Under these sales and services contracts, the cigarette manufacturers and tobacco redrying factories are sometimes entitled to withhold the remaining 10% of the contract value until the expiration of the warranty period, which usually lasts for 12 months after the acceptance of our products and services. Our customers normally settle their payments by telegraphic transfer.

No provision for warranty in respect of the machinery products sold by us was made during the Track Record Period.

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RAW MATERIALS AND SUPPLIERS

The major raw materials, parts and components used to manufacture our tobacco machinery products include specialised metallic items, counter modules, steel plates and pipes, electronic devices as well as instruments and meters, all of which are procured from local suppliers in the PRC. These materials, parts and components are not raw material commodities but principally represent items with specialised functions. We normally submit project proposals to our customers in respect of each project based on the price quotation of the materials, parts and components obtained from the suppliers. Therefore, to a great extent, the fluctuation in the prices of the materials, parts and components would not materially affect our profitability. During the Track Record Period, we did not experience any significant price fluctuations in our major materials, parts and components. As we conduct our business on a project basis, we normally maintain minimum inventory level and will procure the necessary raw materials, parts and components based on the implementation plan of each project.

During the Track Record Period, our aggregate purchases of raw materials, parts and components amounted to approximately HK\$46,922,000, HK\$53,149,000 and HK\$76,817,000 respectively. Raw material, part and component costs represented the largest component of our cost of sales, accounting for approximately 86.6%, 86.7% and 89.7% of our cost of sales for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. During the Track Record Period, the costs of specialised metallic items accounted for approximately 50.4%, 49.6% and 63.2% of our total raw material, part and component costs respectively. Our Group uses a variety of specialised metallic items which include valves, gear pumps, stainless steel pipes, bearings, speed reducers, motors, pneumatic components, weighing sensors and blenders.

The aggregate purchases from our five largest suppliers during the Track Record Period represented approximately 46.9%, 42.4% and 72.8% respectively of our total purchases. During the Track Record Period, purchases from our largest supplier accounted for approximately 10.0%, 13.3% and 35.6% respectively of our total purchases. We have maintained business relationships with our five largest suppliers for approximately 1 to 9 years. None of our Directors or any of their respective associates or any Shareholders (who or which, to the knowledge of our Directors, held 5% or more of the issued share capital of the Company as at the Latest Practicable Date) had any interest in any of our five largest suppliers during the Track Record Period.

We do not rely on any single supplier for any of its raw materials, parts or components. As the raw materials, parts and components sourced are available in the market from a number of alternative suppliers, we do not expect any disruption or difficulty if any of our major suppliers fail to meet our demand. Up to the Latest Practicable Date, we have not experienced any major interruption in the supply of the major materials, parts or components.

We have not entered into any long-term contract with our suppliers, and negotiate the terms of the purchases with our suppliers on a transaction by transaction basis. The normal credit period varies according to the payment terms of different suppliers. The credit periods granted by our suppliers range from 30 to 90 days. Normally, payments are made by us to our suppliers by electronic transfer. During the Track Record Period, the raw materials, parts and components sourced from suppliers were denominated in Renminbi.

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Our procurement department procures our raw materials, parts and components based on the requirements of our projects taking into account the raw materials, parts and components in stock. We maintain a list of approved suppliers and we procure our raw materials, parts and components from such suppliers. Our procurement department will compare the raw materials, parts and components supplied by at least three approved suppliers and select the most suitable supplier based on the pricing, quality, payment terms and the ability to deliver the materials, parts and components on time. In the selection of our approved suppliers, we take into account different factors including but not limited to the pricing and quality of the raw materials, parts and components, stability of supply and delivery, the credit period offered by the suppliers as well as their reputation. We generally review the list of approved suppliers on an annual basis.

PRODUCTION

Production facilities and production capacity

Our sole manufacturing facility is located on a piece of land with a site area of approximately 62,741 sq.m. in Baoying County, Jiangsu Province, the PRC on which five buildings occupying total gross floor area of approximately 26,986 sq.m. were erected. Our factory area was approximately 23,223 sq.m. as at the Latest Practicable Date.

Generally, it is difficult for us to accurately estimate the production capacity and the actual utilisation rate of our production facilities for each of our products as (i) our business is project based and our products are highly customised; (ii) the time needed for completing our projects which may vary from 1 month to 9 months depending on the size of our projects which may differ significantly with the type of products and services provided as well as the complexity of our clients' requirements; and (iii) the number of projects completed every year with respect to each of our products is not predictable. We generally estimate our production capacity based on the number of total working hours of our production staff during the year. For each of the two years ended 31 December 2010 and the six months ended 30 June 2011, we had 3 production teams with a total of 51, 52 and 54 workers respectively. Based on 250 working days in a year and 8 normal working hours in a day, the total working hours of our production staff were 102,000, 104,000 and 52,704 for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. Utilisation rates are estimated primarily according to the actual working time of our production staff as compared with their total working hours during the year/period. The actual working time of our production staff is determined based on the actual projects undertaken in the relevant year/period and the number of working hours required for the relevant projects. During the Track Record Period, we estimate that our utilisation rate was approximately 93.9%, 111.0% and 134.2% respectively. The substantial increase in the utilisation rates in 2010 and the first half of 2011 was mainly due to the increase in our business volume. Utilisation rate over 100% represented overtime operation of our production staff and the increase in our subcontracting volume in 2010 and the first half of 2011.

We currently intend to expand our production capacity by recruiting additional workers. We do not expect any difficulty in hiring employees with the requisite skills to carrying out our production procedures which include raw material cutting, drilling, bending and welding. We may also outsource parts of our production processes to subcontractors in order to cope with our production needs. Please refer to the paragraph headed "Production – outsourcing" of this section for further details in respect of our subcontractors. We will continue to evaluate our production needs and utilise our internal resources to proceed with such expansion so as to cope with our business development as and when required.

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Outsourcing

We engage an independent subcontractor to work on the processing and manufacturing of certain parts and components for our casing and flavouring systems at our production facilities, as well as assembly and installation of our casing and flavouring systems at the production sites of the cigarette manufacturers. As our business is project based, we consider that such subcontracting services would facilitate our efforts to satisfy our production requirements in accordance with the implementation plan of a project in a cost-effective manner. The major terms and conditions of such subcontracting arrangements include, among others:

- the subcontractor assigns workers to our production site based on the requirements of individual projects to collaborate with our staff for the production and installation of our products;
- the subcontractor has to strictly comply with our technical requirements and its production process is subject to our supervision and testing;
- the subcontractor has to keep our business secrets and all information in relation to our products in strict confidence; and
- the services fee is subject to pre-agreed service fee guidelines contained in the subcontracting agreement, which sets out the processing and assembly unit fee.

The subcontractor is required to meet our quality standards in performing its work. The products processed and installed by the subcontractor are subject to our quality inspection and the subcontractor is responsible for rectifying any quality defects in such products as identified by our Group.

In addition, we engage two other independent subcontractors to work on surface processing which include painting and sand blasting.

Basically, we select the subcontractors based on a number of criteria including but not limited to the credit period, quality of their services and the payment terms offered. We believe that we do not rely on any single subcontractor as we can easily identify alternative subcontractors offering similar services in the market within a relatively short period of time. Therefore, we do not expect any disruption or difficulty if any of our subcontractors is not able to continue providing their services to us. During the Track Record Period, our subcontracting charges amounted to approximately HK\$1,024,000, HK\$1,345,000 and HK\$912,000 respectively. The rise in the subcontracting charges in 2010 (as compared to that of 2009) and the first six months of 2011 (as compared to that of the corresponding period in 2010) was mainly due to increases in the subcontracting volume. We have maintained business relationships with our existing subcontractors for approximately 7 months to 2 years. None of our Directors or any of their respective associates or any Shareholders (who or which, to the knowledge of our Directors, held 5% or more of the issued share capital of the Company as at the Latest Practicable Date) had any interest in any of our subcontractors during the Track Record Period.

QUALITY CONTROL

We are committed to providing products and services with high quality standards. We have adopted quality control and assurance procedures throughout our production process, from the sourcing of raw materials, parts and components to the production processes. Our quality control team is responsible for implementing quality assurance at every stage of the production process at our manufacturing facilities while our technical personnel will conduct quality inspections during the product installation process at the customers' sites. As at 31 August 2011, our quality control department comprised 4 staff members who possess experience ranged from 2 years to 10 years in the tobacco machinery industry.

As a recognition to the quality of our production process, we have been awarded ISO 9001:2008 certification by World Standards Certification Center Inc. in respect of our quality management system for the design, production and sales of electrical system for tobacco cutting production line, casing and flavouring system and cut tobacco feeding system. Our ISO certification remains valid up till June 2012.

We implement quality assurance measures in the following areas:

(i) Selection of suppliers

Raw materials, parts and components are purchased from approved suppliers. In the selection of our suppliers, we take into account different factors including but not limited to the quality of the raw materials, parts and components, stability of supply and delivery as well as the reputation of the suppliers. We would request for samples of the raw materials, parts and components to be supplied in order to ensure that the raw materials, parts and components meet our requirements.

(ii) Quality control of raw materials, parts and components

Our quality control personnel carry out inspections on every batch of raw materials, parts and components when they are delivered to our production site from the suppliers to ensure that they meet our required quality standards. Quality checking reports will be prepared by our quality control team. Any raw materials, parts and components which do not meet our quality standards and specifications are returned to the relevant suppliers.

(iii) Quality control during the production process

We regularly inspect our production facilities and production machinery to ensure reliable operation. During each stage of the production process, we carry out inspections and performance tests to ensure compliance with our quality assurance measures. Our quality control personnel normally inspect 100% of the semi-finished products at each stage of the production process. Any items which cannot pass the quality check will be either discarded or reprocessed depending on the severity and type of error.

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(iv) Quality control on the finished products

After the semi-finished products as well as procured parts and components are delivered to the production sites of the cigarette manufacturers or tobacco redrying factories, we will carry out the assembly, installation, tuning and testing of the products. We will also assist our customers in the integration of the products into their production line for a trial run to ensure that the products function properly in accordance with the customers' requirements. Our products are deemed to be accepted by our customers once a certificate of normal operation is signed by the cigarette manufacturers or tobacco redrying factories.

As a result of our stringent quality control system, we have not experienced any product complaint or return due to product quality problems up to the Latest Practicable Date.

We estimate that the average replacement cycle of our tobacco machinery products is around 8 years, provided that regular inspections and maintenance of the machinery are performed by our customers during such period to ensure their normal operation. Notwithstanding the above, given the fact that our Group only commenced the manufacturing of tobacco machinery products since November 2001, we do not have a long operating history as compared to the replacement cycle of our products that enables us to ascertain whether we will obtain repeating orders from our existing customers or whether they will select our products for replacement in the future.

TOBACCO PRODUCTION LICENCE

Under relevant PRC regulations, domestic manufacturers engaging in the production of tobacco machinery as listed on the Tobacco Machinery List must possess the Tobacco Production Licence to manufacture and sell the relevant tobacco machinery. According to the Measures on Administration of Tobacco Monopoly Licence, enterprises applying for the Tobacco Production Licence have to satisfy the following conditions: (i) maintaining adequate funds for the production of tobacco monopoly commodities; (ii) possessing the necessary technology and equipment for the production of tobacco monopoly commodities; (iii) meeting the requirements of national policies in respect of the tobacco industry and conducting corporate restructuring when necessary; and (iv) satisfying any other conditions set by the department of tobacco monopoly administration under the State Council.

We have obtained a Tobacco Production Licence under which we are permitted to manufacture, sell and provide maintenance, overhaul as well as modification services in respect of casing and flavouring systems, feeding systems and PP systems. Our Directors believe that we are able to satisfy the aforesaid conditions for applying the Tobacco Production Licence as (i) the registered capital of Baoying Renheng of RMB42,857,142.86 provides our Group with sufficient funds required for the production of the catalogued special-purpose tobacco machinery set out in our Tobacco Production Licence; (ii) we have obtained proprietary or legally authorised intellectual property rights over our catalogued special-purpose tobacco machinery; (iii) our senior management team has extensive experience in the tobacco machinery manufacturing industry or engineering business; (iv) we have set up our own plant and equipment required for the production of our catalogued special-purpose tobacco machinery; and (v) we have obtained approval from the Economic Commission, Planning Commission as well as Foreign Trade and Economic Relations Commission of Baoying County to engage in, among others, the production of tobacco machinery since October 2001. Our current licence is valid for a period of five years commenced from 14 April 2009 and will expire on 14 April 2014.

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As advised by the PRC Legal Advisers, provided that there is no change in Baoying Renheng's corporate capacity under the law of the PRC, we can maintain our Tobacco Production Licence and carry on the production of our catalogued special-purpose tobacco machinery. The PRC Legal Advisers have also advised that we can apply for renewal of our Tobacco Production Licence if we are able to maintain our production and operational capabilities without any significant change and if we are not involved in any material non-compliance incidents. We have not experienced any difficulty in obtaining renewal of our Tobacco Production Licence in the past. As advised by the PRC Legal Advisers, we have complied with the requirements under the Measures on Administration of Tobacco Monopoly Licence and the respective notices on the renewal of Tobacco Production Licence issued by STMA in 2003 and 2008 regarding renewal of our Tobacco Production Licence. In addition, Baoying Renheng has obtained a confirmation issued by STMA dated 9 March 2011 which states that, since 15 January 2002 and up to the date of the confirmation, Baoying Renheng possessed a valid Tobacco Production Licence in carrying out its business.

We have designated one of our executive Directors, Mr. Sun Zhaohui, who is also the legal representative of Baoying Renheng, to monitor and ensure our continuous fulfillment of the relevant requirements for maintaining the Tobacco Production Licence by (i) maintaining at least the current registered capital of Baoying Renheng; (ii) engaging in continuous product development and innovation; (iii) maintaining adequate personnel for our business operation; (iv) upgrading our production facilities; and (v) expanding our product range and introducing new and enhanced series of tobacco machinery products. During the Track Record Period, we did not incur any direct costs with respect to the maintenance of the Tobacco Production Licence. CTMC conducted an inspection on our Group in 2006. We did not receive any follow-up comment from CTMC. No inspection was conducted by STMA or local tobacco monopoly authorities on our Group during the Track Record Period. For more information about the relevant laws, rules and regulations in relation to Tobacco Production Licence, please refer to the section headed "Regulatory overview" in this prospectus.

RESEARCH AND DEVELOPMENT

We believe that the users of our products, being mainly cigarette manufacturers in the PRC, are focused on continuous technological improvements in their cigarette production process. As a result, we must continuously develop new and innovative products in order to maintain our competitiveness. We are dedicated to the continuous improvement of our design and product development capabilities as well as the quality and reliability of our products. Our technical personnel are responsible for the research and development of our products. As at 31 August 2011, we had 37 technical personnel, out of which 26 are university graduates.

As our business is project based and all of our products are customised, our marketing personnel and technical personnel seek to maintain close contacts with the cigarette manufacturers and tobacco redrying factories in order to have better understanding of their evolving requirements and to keep abreast of the latest market trends. The feedback from the cigarette manufacturers and tobacco redrying factories would enable us to respond more quickly to their demands.

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To enhance our research capability, we entered into a research collaboration agreement with Nanjing University of Science and Technology on 18 March 2008 for a term of 26 months to develop a new type of spraying device to be equipped with our casing and flavouring systems. Pursuant to the agreement, we were responsible for the payment of RMB700,000 in research and development expenses and the provision of certain technical support while Nanjing University of Science and Technology was responsible for undertaking the actual research and development work. In September 2010, we have obtained a jointly owned utility patent in the PRC with Nanjing University of Science and Technology with respect to a vertical pneumatic spraying device (立式氣動混合加香加料裝置) and have applied for the registration of a jointly owned invention patent regarding this spraying device in the PRC. Such device aims to allow the spraying of the processed casing and flavour mixtures onto the cut tobacco in a more evenly manner during the cigarette production process. We are currently under negotiation with Nanjing University of Science and Technology to renew our research collaboration agreement to continue the development of the spraying device.

During the Track Record Period, our total product research and development expenditures amounted to approximately HK\$246,000, HK\$394,000 and HK\$717,000 respectively, which represented approximately 0.3%, 0.4% and 1.1% respectively of our total turnover. We believe that the users of our products, being mainly cigarette manufacturers in the PRC, are focused on continuous technological improvements in their cigarette production process. As a result, in order to maintain our competitiveness, our Directors intend to apply approximately 71.2% of the net proceeds from the Placing on continuous product development and innovation, despite the small amounts of product research and development expenditures recorded during the Track Record Period. We plan to expand our product range and create new and enhanced series of catalogued special-purpose tobacco machinery products with innovative designs to meet the evolving requirements of cigarette manufacturers and tobacco redrying factories. We also intend to expand our scope of catalogued special-purpose tobacco machinery products and launch two research and development programs related to the development of (i) tobacco bale slicer designed for use by the cigarette manufacturers in slicing unwrapped tobacco bale into slices of required sizes for subsequent tobacco processing; and (ii) tobacco redrying system designed for use by tobacco redrying factories in the redrying process. For further details, please refer to the paragraph headed “Reasons for the Placing and use of proceeds” in the section headed “Future plans and prospects” in this prospectus.

INTELLECTUAL PROPERTY

In order to protect our rights over the intellectual property of the products and technologies invented and developed by us or jointly with independent third parties, we have obtained 7 patents registered in the PRC (including 1 design patent and 6 utility patents), of which 5 are solely owned patents and 2 are jointly owned patents. We have also obtained a trade mark registration in Hong Kong. We have applied for the registration of 8 jointly owned patents in the PRC. Please refer to the paragraph headed “Intellectual property rights of the Group” in Appendix V to this prospectus for details of the registrations and application for registration of our patents and trademark as at the Latest Practicable Date. As advised by the PRC Legal Advisers, according to relevant PRC laws and regulations, design patents refer to the design of the shape and colour applied to an industrial product. Invention patents refer to the new technical plan proposed for an industrial product or method or modification of such product or method. Utility patents refer to the new technical method regarding the shape and structure utilised for an industrial product.

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“仁恒” has been registered as a trademark under the class of property development in the PRC in 2003 by a Singaporean company which is engaged in property development. However, as advised by the PRC Legal Advisers, taking into account that (i) Baoying Renheng has obtained approval from the local administration of industry and commerce for registration of its company name prior to the registration of “仁恒” as a registered trademark by the Singaporean company; (ii) Baoying Renheng commenced to use the name “仁恒” as its company name on 1 November 2001 (being the date on which Baoying Renheng was established and obtained its business licence) prior to the date the Singaporean company obtained the right to exclusive use of the registered trademark of “仁恒” in 2003; and (iii) the use of “仁恒” as the company name by Baoying Renheng which has principally been engaged in the manufacture and sale of catalogued special-purpose tobacco machinery since its establishment shall not create any confusion among purchasers of catalogued special-purpose tobacco machinery with the trademark of “仁恒” registered under the class of property development, the PRC Legal Advisers are of the opinion that not only Baoying Renheng has not infringed upon the right to exclusive use of the registered trademark of “仁恒”, Baoying Renheng has the right to continue using “仁恒” as its company name in compliance with relevant laws and regulations and the Singaporean company has no right to apply for revocation of the registration of Baoying Renheng’s company name.

During the Track Record Period, we did not experience any counterfeiting of our products or infringement of our intellectual property rights by any third party, or violate or face any claims relating to the intellectual property rights of any third party.

As at the Latest Practicable Date, we were the registrant of the domain names of renhengenterprise.com, renhengenterprise.com.hk, renheng.com.hk and renhengenterprise.com.cn.

AWARDS AND RECOGNITION

We have been awarded a number of awards and certifications by various organisations, all of them being Independent Third Parties. Set out below is a list of the major awards and certifications awarded by various governmental authorities in the PRC in the past:

Year of grant	Award or certification	Awarding association
2003	Advanced Technological Work Unit (企業科技工作先進單位)	People’s Government of Baoying County (寶應縣人民政府)
2005	High and New Technology Enterprise Certificate (高新技術企業認定證書)	Science and Technology Department of Jiangsu Province (江蘇省科學技術廳)
2006	Award of Automatic Tobacco-related Casing and Flavouring System (煙用糖料香料自動調配及自動加香加料裝置獲獎證書)	People’s Government of Yangzhou City (揚州市人民政府)
2009	The Enterprise Honouring Contracts and Credit (重合同守信用企業)	Administration for Industry and Commerce of Yangzhou, Jiangsu Province (江蘇省揚州工商行政管理局)

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PROPERTIES

Owned properties

We own our sole manufacturing facility in Baoying County, Yangzhou, Jiangsu Province, the PRC. The property comprises the New Land with a site area of approximately 62,741 sq.m. for which we have obtained the relevant State-owned land use rights certificate for a term expiring on 6 June 2054 for industrial use and five buildings occupying a total gross floor area of approximately 26,986 sq.m. We have obtained the relevant building ownership certificates for all such buildings. The property is currently occupied by Baoying Renheng for production, storage, dormitory and ancillary office purposes except for portions of the property which are leased to two related parties.

We have leased a portion of an industrial building with a gross floor area of approximately 4,800 sq.m. to Longtai for a term of 2 years commencing from 1 January 2011 to 31 December 2012 at a monthly rental of RMB28,800 which was determined by the parties with reference to the then prevailing rental market condition of comparable premises. Another portion of the same building with a gross floor area of approximately 5,040 sq.m. is leased to Jinchuang for a term of 2 years commencing from 1 January 2011 to 31 December 2012 at a monthly rental of RMB30,240 which was determined by the parties with reference to the then prevailing rental market condition of comparable premises. Each of Longtai and Jinchuang is a related party of our Group. For further information, please refer to the section headed “Connected transactions” in this prospectus.

Leased property

We have leased and occupy a premises with a gross floor area of about 60.94 sq.m. at Room 1303, 13th Floor, Keen Hung Commercial Building, 80 Queen’s Road East, Wanchai, Hong Kong for a term of 2 years commenced from 17 January 2011 and expiring on 16 January 2013 at a monthly rental of HK\$13,770 inclusive of rates and management fee. The leased premises has been used by us as office premises.

Greater China Appraisal Limited, an independent property valuer, has prepared a valuation report in respect of our owned and leased properties as set out in Appendix III to this prospectus.

SAFETY AND ENVIRONMENTAL MATTERS

Workplace safety

We are subject to relevant PRC laws and regulations regarding production safety, including the principle law governing the administration of production safety in the PRC, namely PRC Production Safety Law (中華人民共和國安全生產法) which took effect on 1 November 2002. We have set up a safety supervision division to implement production safety as well as fire control safety measures. A written document covering the composition and responsibilities of our safety supervision division, measures relating to fire control as well as the standard operation procedures with regard to various types of machinery has been issued and displayed in a prominent place in our production facilities for the workers. We also carry out inspections on our production facilities on a daily basis to identify any potential production safety problem arising from our daily operation. Our Directors consider

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that we have implemented sufficient measures to ensure our compliance with the relevant laws and regulations in the PRC relating to production safety as we did not violate any relevant production safety laws and regulations during the Track Record Period. There was no material accident during our production process during the Track Record Period.

Environmental issues

Our operations in the PRC are subject to environmental protection laws and regulations promulgated by the PRC government. The pollutants generated during our production process include waste water, exhausted gas and noise. We have installed the necessary environmental protection facilities to comply with the relevant environmental laws, rules and regulations in the PRC. Baoying Renheng did not obtain the environmental protection facilities approval prior to the commencement of its trial operations at the current production site in 2005 but has subsequently obtained the environmental protection facilities approval issued by the Environmental Protection Bureau of Yangzhou (揚州市環境保護局) dated 28 January 2008. The PRC Legal Advisers are of the opinion that since Baoying Renheng has not been ordered by the relevant authority to rectify the aforesaid non-compliance incident, Baoying Renheng would not be ordered to suspend operations or penalised for not obtaining the environmental protection facilities approval prior to the commencement of trial operations. Furthermore, having considered that Baoying Renheng has obtained (i) approval from the relevant authority for an environmental impact assessment before commencement of the construction work on the relevant property; and (ii) the environmental protection facilities approval issued by the Environmental Protection Bureau of Yangzhou dated 28 January 2008, the PRC Legal Advisers are of the opinion that Baoying Renheng has complied with the requirements of the relevant construction project environmental protection regulations. We hold a pollutant emission permit (排放污染物許可證) issued by the Environmental Protection Bureau of Baoying (寶應縣環境保護局) dated 1 January 2011 in respect of the waste water, exhaust gases and noise generated during our production process for a term of one year commencing from 1 January 2011 and expiring on 31 December 2011. The pollutant emission permit is subject to annual review by the relevant environmental protection bureau. We have not experienced any difficulty in obtaining renewal of our pollution emission permit in the past.

As advised by the PRC Legal Advisers, Baoying Renheng has obtained a certificate issued by the Environmental Protection Bureau of Baoying (寶應縣環境保護局) dated 28 October 2010 which states that, since its establishment up to the date of the certificate, Baoying Renheng (i) has complied with the relevant environmental protection laws and regulations; (ii) obtained relevant approval with respect to environmental protection; (iii) has complied with the applicable national standards in relation to the emission of pollutants generated during its production process such as waste water, dust and noise; (iv) has not caused any environmental pollution; and (v) has not been subject to any penalty imposed by the Environmental Protection Bureau of Baoying.

The PRC Legal Advisers have also confirmed that (i) save for the failure in obtaining the environmental protection facilities approval prior to the commencement of its trial operations at the current production site in 2005, Baoying Renheng has complied with the relevant environmental protection laws, rules and regulations in the PRC; and (ii) no penalties regarding environmental protection was imposed on Baoying Renheng by any relevant environmental protection authorities in the PRC as a result of non-compliance act in breach of environmental protection laws, rules or regulations in the PRC.

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During the Track Record Period, we incurred expenses in respect of environmental compliance matters of approximately HK\$12,000, HK\$13,000 and HK\$10,000 respectively. We currently expect our cost of compliance to remain at similar levels going forward.

INSURANCE

We maintain property insurance coverage against the losses arising from damages to our fixed assets and inventories due to accidents such as power failure, suspension of water supply and gas shortage as well as natural disasters. We have mandatory automobile liability insurance for all our vehicles in use in respect of third party liability risks. We also maintain mandatory social insurance for our employees as required under PRC laws to provide for pension, medical, unemployment, work-related injury and maternity benefits. Our Directors believe that our existing insurance coverage is in line with the general practice in the PRC tobacco machinery industry and is sufficient for our operations. During the Track Record Period, we had not been the subject of any material insurance claim.

We do not maintain any product liability insurance as there is no mandatory requirement in the PRC to maintain such insurance. During the Track Record Period, we did not receive any product liability claim.

LEGAL PROCEEDINGS

During the Track Record Period and as at the Latest Practicable Date, we have not been engaged in any litigation, arbitration or claim of material importance, and no litigation, arbitration or claim was known to our Directors to be pending or threatened by or against us, that would have a material adverse effect on our operation results, or financial condition, taken as a whole.

COMPETITION

All manufacturers engaging in the sale and production of catalogued special-purpose tobacco machinery in the PRC have to obtain the Tobacco Production Licence. We believe that the licensing regime itself creates a barrier of entry. Competition in the PRC catalogued special-purpose tobacco machinery industry is relatively moderate due to the limited number of participants. According to the China Tobacco Year Book 2008 published by STMA in January 2010, as at the end of 2008, there were 36 tobacco machinery manufacturers which have been granted the Tobacco Production Licence. Each of these licenced manufacturers was permitted to engage in the manufacture, sale and provision of maintenance, overhaul and modification services in one or more types of catalogued special-purpose tobacco machinery as listed on the Tobacco Machinery List. The number of tobacco machinery manufacturers which were permitted to engage in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of casing and flavouring systems, feeding systems and PP systems were 6, 18 and 3 respectively. PF system is a sub-class of feeding system listed on the Tobacco Machinery List. To the best of our Directors' knowledge, information and belief, there were about 3 domestic competitors engaged in the manufacture and sale of PF system as at the end of 2008. On the other hand, there were 17 tobacco machinery manufactures whose Tobacco Production Licence did not cover the manufacture and sale of casing and flavouring systems, feeding systems and PP systems.

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Based on the China Tobacco Year Book 2009 published in December 2010, the number of tobacco machinery manufacturers which have been granted the Tobacco Production Licence was reduced to 34 as at the end of 2009. As the two dropped out manufacturers which no longer possessed the Tobacco Production Licence were not permitted to engage in the manufacture and sale of casing and flavouring systems, PF systems and PP systems, to the best of our Directors' knowledge, information and belief, the number of domestic competitors engaged in the manufacture and sale of casing and flavouring systems, PF systems and PP systems remained at 6, 3 and 3 as at the Latest Practicable Date.

Under relevant PRC regulations, procurements of tobacco machinery products from foreign suppliers have to be approved by STMA and conducted through China Tobacco Import and Export Company (中國煙草進出口總公司). The Mechanical and Electrical Products Import Office of STMA (國家煙草專賣局機電產品進口辦公室) is responsible for administering the import of tobacco machinery and will make a semi-annual plan for the imports of tobacco machinery with reference to the overall demand of technological transformation in the tobacco industry. We believe that we are able to maintain our competitiveness over foreign manufacturers of casing and flavouring systems, PF systems and PP systems not only because of our relatively closer proximity to our customers, but also due to the fact that we have a better understanding of local market trends and the needs of domestic cigarette manufacturers and tobacco redrying factories, which would enable us to provide more customised products for them.

We compete on the basis of our experience in this industry, our experienced management team, our research and development capabilities, the quality of our products as well as our established long term relationships with the PRC cigarette manufacturers. We expect to further increase our competitiveness by continuous improvement and development of our technology as well as introduction of new products in the future.

CONNECTED TRANSACTIONS

CONNECTED TRANSACTIONS

Summary

During the Track Record Period and prior to the Listing, we entered into various transactions with certain parties which are/were or which we consider to be connected persons as defined under the GEM Listing Rules after the Listing Date, all of which other than as disclosed in the paragraph headed “Continuing connected transactions exempt from reporting, annual review, announcement and independent shareholders’ approval requirements” in this section have been discontinued prior to the Latest Practicable Date. We set out below details of our relationship with these connected persons and the details of these connected transactions.

Connected persons

Under the GEM Listing Rules, the following person/companies are treated as connected persons of our Company due to their relationship with our Group as highlighted below:

- (1) Yanlord Industry Investment is an investment holding company which is held as to 60% by Mr. Wei and 40% by Ms. Liu.
- (2) Jinchuang is a wholly owned subsidiary of Yanlord Industry Investment. Jinchuang is principally engaged in (i) the manufacture and installation of windows, doors, curtain walls and related products; (ii) the production of composite tubes and related products; and (iii) the processing of metallic products.
- (3) Longtai is a wholly owned subsidiary of Yanlord Industry Investment. Longtai is principally engaged in the production and sale of voltage electrical switchbox, network cabinet, console and control box as well as the provision of related technical consultancy and services.
- (4) Grand Bright is an investment holding company which is held as to 95% by Mr. Wei and 5% by Ms. Liu.

Each of the Controlling Shareholders and Directors does not have any interest in business that competes with our Group.

CONNECTED TRANSACTIONS

DISCONTINUED CONNECTED TRANSACTIONS

Prior to the Latest Practicable Date, our Group had a number of transactions with certain connected persons of our Company. To minimise such transactions, our Group has prior to the Listing discontinued the following transactions:-

(1) Purchase of fixed assets from Longtai

For the year ended 31 December 2010, Baoying Renheng purchased forklift from Longtai in an aggregate amount of approximately HK\$33,000.

(2) Financial assistance by our Group to Longtai

For the year ended 31 December 2009, Baoying Renheng provided interest-free advances of RMB2,120,000 to Longtai. The advances were fully settled by the year ended 31 December 2010. According to the PRC Legal Advisers, any advancing activities between enterprises established in PRC are in breach of 貸款通則 (Loan Regulations) and are subject to the possible penalty imposed by the PBOC of a fine equivalent to 1 to 5 times of the income generated from such advances. Having considered that (i) Baoying Renheng did not generate any income from the said advancing activities; (ii) the advances have been fully settled; and (iii) Baoying Renheng was not engaged in any advancing activities in the PRC as at the Latest Practicable Date, the PRC Legal Advisers are of the view that Baoying Renheng will not be penalised as a result of the said advancing activities.

(3) Financial assistance by Grand Bright and Yanlord Industry Investment to our Group

During the Track Record Period, Grand Bright and Yanlord Industry Investment provided advances of an aggregate amount of approximately HK\$2,878,000 to our Group for payment of professional fees. An amount of approximately HK\$378,000 due to Yanlord Industry Investment was settled with an outstanding amount of HK\$2,500,000 due to Grand Bright as of 31 December 2010. Between March and April 2011, Grand Bright advanced an aggregate amount of HK\$650,000 to our Group for payment of professional fees. In June 2011, the outstanding amount of HK\$3,150,000 due to Grand Bright was fully settled.

(4) Securities provided by Baoying Renheng to Jinchuang

During the Track Record Period, Baoying Renheng provided real estate mortgages up to RMB6 million to a banking institution in the PRC pursuant to two mortgage agreements dated 12 May 2009 (the “**Mortgages**”) executed by Baoying Renheng in favour of the bank to secure banking facilities granted to Jinchuang. The Mortgages were discharged during the year ended 31 December 2010.

CONNECTED TRANSACTIONS

CONTINUING CONNECTED TRANSACTIONS EXEMPT FROM REPORTING, ANNUAL REVIEW, ANNOUNCEMENT AND INDEPENDENT SHAREHOLDERS' APPROVAL REQUIREMENTS

After the Listing Date, our Group will continue to engage in various transactions in the ordinary and usual course of our business with the connected persons of our Company. Each of these transactions will constitute a continuing connected transaction under Rule 20.14 of the GEM Listing Rules.

As each of the applicable percentage ratios (other than the profits ratio) for the below transactions is less than 5% with annual aggregate values below HK\$1 million, the below transactions constitute de minimis continuing connected transaction, which are exempted from the reporting, annual review, announcement and independent shareholders' approval requirements applicable under Chapter 20 of the GEM Listing Rules.

(1) Purchase and sale of switchgear, control switchbox and working platform between our Group and Longtai and provision of subcontracting work from Longtai to our Group

Background

Baoying Renheng purchased certain industrial goods including but not limited to working platform and control switchbox from Longtai during the Track Record Period. The sourcing and purchase of such components was conducted in the ordinary and usual course of business of Baoying Renheng. Agreements were entered into between Baoying Renheng and Longtai during the Track Record Period regarding the aforesaid purchase of goods.

The aggregate purchase value paid by Baoying Renheng to Longtai in respect of the above for the two years ended 31 December 2010 and the six months ended 30 June 2011 were approximately HK\$34,000, HK\$434,000 and HK\$11,000 respectively.

On the other hand, Baoying Renheng also sold certain electrical goods including but not limited to switchgear (work in progress and finished goods), moulds, multi-purpose racks and cabinets to Longtai during the Track Record Period. Agreements were entered into between Baoying Renheng and Longtai during the Track Record Period regarding the aforesaid sale of goods. The sale of such electrical goods was conducted in the ordinary and usual course of business of Baoying Renheng.

The aggregate revenue received by Baoying Renheng from Longtai in respect of the above for the two years ended 31 December 2009 and 2010 and the six months ended 30 June 2011 were approximately HK\$347,000, nil and nil respectively.

Baoying Renheng would also engage Longtai in providing subcontracting work from time to time. During the Track Record Period, Longtai provided subcontracting work, including but not limited to, secondment of Longtai technical staff to Baoying Renheng for installation projects and processing of tobacco machinery parts in an aggregate amount of approximately HK\$113,000 for the year ended 31 December 2010 and approximately HK\$133,000 for the six months ended 30 June 2011 respectively.

CONNECTED TRANSACTIONS

During the Track Record Period, written agreements were entered into between Baoying Renheng and Longtai regarding the sale and purchase of goods and the subcontracting services. The prices of the goods and the fees for the services were agreed by the relevant parties with reference to, among other things, the terms offered to/by our Group by/to Independent Third Parties and at the then prevailing prices of the goods and the prevailing fees of the services. The agreed prices and the agreed fees were generally no less favourable than the then prevailing prices of the relevant goods and the prevailing fees of the relevant services available in the market. Our Directors confirmed that the historical transactions were conducted on an arm's length basis and were no less favourable than the then prevailing market prices.

Baoying Renheng and Longtai will continue to sell or purchase goods from each other and Baoying Renheng will continue to engage Longtai in providing subcontracting services after the Listing. On 18 October 2011, Baoying Renheng and Longtai entered into a master agreement for the sale and purchase of the aforesaid goods and the subcontracting services for a term of three years commencing from the Listing Date for the purpose of formalising the business relationship between Baoying Renheng and Longtai.

Based on the anticipated sale and purchase value of the goods and the subcontracting services, our Directors estimate that the annual aggregate values of such sale and purchase payable or receivable by Baoying Renheng for each of the three years ending 31 December 2011, 2012 and 2013 will not exceed HK\$1,000,000.

(2) **Lease of the Baoying Renheng office**

(a) *The Longtai Lease*

On 16 June 2009, Baoying Renheng and Longtai entered into a tenancy agreement (the “**2009 Longtai Lease**”) for the lease by Baoying Renheng of 7,233 square metres of its part office premises situate at No. 18, Suzhong North Road, Baoying County, Jiangsu Province, PRC to Longtai for a period of five (5) years starting from 1 August 2007 to 1 August 2012. Pursuant to the 2009 Longtai Lease, the rental payable by Longtai for the three years ended 31 July 2008, 2009 and 2010 was fixed at RMB 4 per sq.m per month, i.e. RMB345,600 per annum whilst the rental payable for the two years ending 31 July 2011 and 2012 shall be determined by the parties by taking reference of the prevailing rental market condition of comparable premises at material time. The then prevailing market rate was RMB6 per sq.m. at the time of entering into the lease but Baoying Renheng offered a better rate to Longtai under the 2009 Longtai Lease because Baoying Renheng from time to time would purchase switchgear, control switchbox and subcontract the manufacture of switchgear to Longtai. The proximity allowed Baoying Renheng to monitor the production process and ensure product quality. This would also cut down transportation costs.

CONNECTED TRANSACTIONS

Baoying Renheng entered into a new tenancy agreement with Longtai on 1 January 2011 for a period of two (2) years starting from 1 January 2011 to 31 December 2012 (the “**New Longtai Lease**”) which superseded the 2009 Longtai Lease. Pursuant to the New Longtai Lease, the rental payable by Longtai for the two years ending 31 December 2011 and 2012 is calculated on the basis of RMB6 per sq.m. with a leased area of 4,800 sq.m., i.e. RMB345,600 per annum which was determined by the parties by taking reference of the prevailing rental market condition of comparable premises at material time.

For the two years ended 31 December 2009 and 2010 and the six months ended 30 June 2011, our Group recorded rental income from Longtai of approximately HK\$392,000, HK\$400,000 and HK\$206,000 respectively.

(b) The Jinchuang Lease

Baoying Renheng and Jinchuang entered into a tenancy agreement (the “**2008 Jinchuang Lease**”) with effect from 1 January 2008 for the lease by Baoying Renheng of 7,560 square metres of its part office premises situate at No. 18, Suzhong North Road, Baoying County, Jiangsu Province, PRC to Jinchuang for a period of ten (10) years starting from 1 January 2008 to 31 December 2017. Pursuant to the 2008 Jinchuang Lease, the rental payable by Jinchuang for the three years ended 31 December 2008, 2009 and 2010 was fixed at RMB4 per sq.m. per month, i.e. RMB362,880 per annum whilst the rental payable for the rest of the term shall be determined by the parties by taking reference of the prevailing rental market condition of comparable premises at material time. The then prevailing market rate was RMB6 per sq.m. at the time of entering into the lease but Baoying Renheng offered a better rate to Jinchuang under the 2008 Jinchuang Lease because Baoying Renheng was able to receive income from idle factory area with minimum risk of recoverability due to the close relationship with Jinchuang.

Baoying Renheng entered into a new tenancy agreement with Jinchuang on 1 January 2011 for a period of two (2) years starting from 1 January 2011 to 31 December 2012 (the “**New Jinchuang Lease**”) which superseded the 2008 Jinchuang Lease. Pursuant to the New Jinchuang Lease, the rental payable by Jinchuang for the two years ended 31 December 2011 and 2012 is calculated on the basis of RMB6 per sq.m. with a leased area of 5,040 sq.m., i.e. RMB362,880 per annum which is determined by the parties by taking reference of the prevailing rental market condition of comparable premises at material time.

For the two years ended 31 December 2009 and 2010 and the six months ended 30 June 2011, our Group recorded rental income from Jinchuang of approximately HK\$412,000, HK\$419,000 and HK\$216,000 respectively.

FINANCIAL INFORMATION

Potential investors of the Placing Shares should read this section in conjunction with our audited consolidated financial statements for each of the two years ended 31 December 2010 and the six months ended 30 June 2011 and the accompanying notes thereto, the text of which is set forth in the accountants' report in Appendix I to this prospectus. Our consolidated financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards. Potential investors should read the whole of the accountants' report set out in Appendix I to this prospectus and not rely merely on the information contained in this section. The following discussion and analysis contains certain forward-looking statements and information that involve risks and uncertainties. For additional information regarding these risks and uncertainties, please refer to the section headed "Risk factors" in this prospectus.

OVERVIEW

We are principally engaged in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of tobacco machinery products and services. We generate our turnover primarily from three types of catalogued special-purpose tobacco machinery products as listed in the Tobacco Machinery Documents, namely casing and flavouring systems, PF systems and PP systems, and related components and devices not listed on all of the Tobacco Machinery Documents, which accounted for approximately 92.6%, 95.4% and 93.0% of our turnover for each of the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. Our turnover of catalogued special-purposed tobacco machinery projects also includes that derived from sales of parts and sales of components and/or devices which are not listed in the Tobacco Machinery Documents and are not contracted with CTMC but form integral parts of the customised systems. Our non-catalogued ancillary tobacco machinery products and services mainly include dedusting systems and swelling agent delivery systems. We conduct our tobacco machinery product business on a project basis and all of our products are custom-made to meet the needs of cigarette manufacturers and tobacco redrying factories in the PRC.

During the Track Record Period, our turnover amounted to approximately HK\$72,616,000, HK\$91,713,000 and HK\$64,651,000 respectively, and our profit for the year/period was approximately HK\$10,985,000, HK\$19,933,000 and HK\$3,618,000 respectively.

BASIS OF PREPARATION OF FINANCIAL INFORMATION

Our Company was incorporated in the Cayman Islands with limited liability on 2 February 2011 under the Companies Law. Our Group resulting from the Reorganisation is regarded as a continuing entity. Accordingly, the consolidated statements of comprehensive income and cash flows for the two years ended 31 December 2010 and the six months ended 30 June 2011 include the results and cash flows of the companies now comprising our Group, as if our Group structure upon the completion of the Reorganisation had been in existence throughout the two years ended 31 December 2010 and the six months ended 30 June 2011, or since their respective dates of incorporation where this is a shorter period. The consolidated statements of financial position as at 31 December 2009 and 2010 and 30 June 2011 have been prepared to present the assets and liabilities of the entities now comprising our Group as at the respective dates.

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MAJOR FACTORS AFFECTING OUR GROUP'S RESULTS OF OPERATIONS

The major factors which we believe may affect our Group's results of operations include:

Types of projects undertaken

We conduct our tobacco machinery product business on a project basis and the number of projects undertaken every year with respect to each of our products is not predictable. During the Track Record Period, we generated the majority of our turnover from the manufacture, sale and provision of maintenance, overhaul and modification services in respect of three types of catalogued special-purpose tobacco machinery products, namely casing and flavouring systems, PF systems and PP systems, and related components and devices not listed on all of the Tobacco Machinery Documents whilst a minority of our turnover was derived from the manufacture, sale and provision of maintenance, overhaul and modification services in respect of non-catalogued ancillary tobacco machinery products. Our different product categories have historically experienced different gross margins. The following table sets forth our gross profit and gross profit margin by project category during the Track Record Period:

	For the year ended 31 December						Six months ended 30 June					
	2009			2010			2010			2011		
			Percentage			Percentage			Percentage			Percentage
	Gross	profit	of total	Gross	profit	of total	Gross	profit	of total	Gross	profit	of total
	profit	margin	gross	profit	margin	gross	profit	margin	gross	profit	margin	gross
HK\$'000	%	%	HK\$'000	%	%	HK\$'000	%	%	HK\$'000	%	%	
Catalogued special-purpose tobacco machinery projects												
Casing and flavouring systems	16,642	33.9	58.6	22,407	36.6	55.2	4,778	26.9	49.1	17,343	30.2	83.1
PF systems	7,834	63.2	27.6	11,706	65.7	28.8	4,242	66.2	43.6	1,431	57.8	6.8
PP systems	1,739	30.7	6.1	4,773	56.3	11.8	401	78.6	4.1	119	43.4	0.6
	<u>26,215</u>	<u>39.0</u>	<u>92.3</u>	<u>38,886</u>	<u>44.5</u>	<u>95.8</u>	<u>9,421</u>	<u>38.2</u>	<u>96.8</u>	<u>18,893</u>	<u>31.4</u>	<u>90.5</u>
Non-catalogued ancillary tobacco machinery projects and other products												
	<u>2,206</u>	40.9	<u>7.7</u>	<u>1,728</u>	40.7	<u>4.2</u>	<u>317</u>	36.4	<u>3.2</u>	<u>1,982</u>	43.8	<u>9.5</u>
Total	<u><u>28,421</u></u>	<u>39.1</u>	<u>100.0</u>	<u>40,614</u>	<u>44.3</u>	<u>100.0</u>	<u>9,738</u>	<u>38.1</u>	<u>100.0</u>	<u>20,875</u>	<u>32.3</u>	<u>100.0</u>

During the Track Record Period, our turnover generated from sales of tobacco machinery amounted to approximately HK\$54,912,000, HK\$66,393,000 and HK\$58,459,000 respectively, while our turnover generated from the provision of maintenance, overhaul and modification services amounted to approximately HK\$17,704,000, HK\$23,699,000 and HK\$3,950,000 respectively.

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In December 2010, we commenced to supply hot stamped foil used in cigarette packaging. The turnover and gross profit derived from the sale of hot stamped foil were approximately HK\$1,621,000 and approximately HK\$472,000 respectively for the year ended 31 December 2010, representing approximately 1.8% of our turnover for the year and a gross profit margin of approximately 29.1% respectively. The corresponding turnover and gross profit increased to approximately HK\$2,242,000 and approximately HK\$798,000 respectively for the six months ended 30 June 2011, representing approximately 3.5% of our turnover for the period and a gross profit margin of approximately 35.6% respectively.

As the gross margins of our products vary, any change in the product mix of our turnover will certainly affect our results of operations from one year to another.

Level of capital spending by cigarette manufacturers and tobacco redrying factories in the PRC

During the Track Record Period, all of our turnover was derived from sales in the PRC. The demand for our tobacco machinery products depends significantly on the level of installing, replacement and maintenance activities of cigarette manufacturers and tobacco redrying factories in the PRC, which in turn depends on the level of capital spending by such cigarette manufacturers and tobacco redrying factories. As discussed in the paragraph headed “Tobacco industry in the PRC – Consolidation of PRC tobacco industry” under the section headed “Industry overview” in this prospectus, the fixed asset investment in the tobacco products industry in urban areas grew at a CAGR of approximately 20.1% between 2004 and 2009 while the fixed asset investment in relation to equipment purchasing in the tobacco products industry increased at a CAGR of approximately 13.5% in the same period. However, there is no assurance that the fixed asset investment in relation to equipment purchasing in the tobacco products industry in the PRC will continue to grow at the same rate as discussed above or that its growth will be steady in the coming future. Any decrease in the level of capital spending by cigarette manufacturers and tobacco redrying factories in the PRC may have a direct impact on our results of operations.

Change in costs of raw materials, parts and components

While we price our catalogued products in accordance with (i) the 5% range of the guidance price in the Pricing Guidelines; and (ii) the Pricing Approval 2010, we determine the contract price based on our estimated project costs plus a mark-up margin at the time we submit a proposal to our potential customers or our tenders for projects. During the Track Record Period, raw material, part and component cost has been the largest component of our cost of sales, accounting for approximately 86.6%, 86.7% and 89.7% of our total cost of sales for each of the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. After we have entered into a sales contract with our customers, we may then procure the necessary raw materials, parts and components. There is a time lapse between the submission of proposals or tenders and the procurement of raw materials, parts and components. Any changes in the prices of raw materials, parts and components during this interim period will affect our profitability.

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Market competition

During the Track Record Period, approximately 92.6%, 95.4% and 93.0% of our turnover was derived from the manufacture, sale and provision of maintenance, overhaul and modification services in respect of catalogued special-purpose tobacco machinery products and related components and devices not listed in all of the Tobacco Machinery Documents. Under relevant PRC regulations, domestic manufacturers engaging in the manufacture and sale of catalogued special-purpose tobacco machinery products in the PRC must possess the Tobacco Production Licence. According to the China Tobacco Year Book 2008 published by STMA in January 2010, as at the year end of 2008, there were 36 tobacco machinery manufacturers which have been granted the Tobacco Production Licence. Each of these licenced manufacturers was permitted to engage in the manufacture, sale and provision of maintenance, overhaul and modification services in one or more types of catalogued special-purpose tobacco machinery as listed on the Tobacco Machinery List. The number of tobacco machinery manufacturers which were permitted to engage in the manufacture, sale and provision of maintenance, overhaul and modification services in respect of casing and flavouring systems, feeding systems and PP systems were 6, 18 and 3 respectively. PF system is a sub-class of feeding system listed on the Tobacco Machinery List. To the best of our Directors' knowledge, information and belief, there were about 3 domestic competitors engaged in the manufacture and sale of PF system as at the end of 2008. On the other hand, there were 17 tobacco machinery manufactures whose Tobacco Production Licence did not cover the manufacture and sale of casing and flavouring systems, feeding systems and PP systems.

Based on the China Tobacco Year Book 2009 published in December 2010, the number of tobacco machinery manufacturers which have been granted the Tobacco Production Licence was reduced to 34 as at the end of 2009. As the two dropped out manufacturers which no longer possessed the Tobacco Production Licence were not permitted to engage in the manufacture and sale of casing and flavouring systems, PF systems and PP systems, to the best of our Directors' knowledge, information and belief, the number of domestic competitors engaged in the manufacture and sale of casing and flavouring systems, PF systems and PP systems remained at 6, 3 and 3 as at the Latest Practicable Date.

During the Track Record Period, our Group was able to record gross profit margin ranging from 31.4% to 44.5% for our catalogued special-purpose tobacco machinery products. Our Directors consider that competition in the PRC catalogued special-purpose tobacco machinery industry is relatively moderate due to the limited number of participants and there are opportunities for catalogued special-purpose tobacco machinery manufacturers to continue to grow.

CRITICAL ACCOUNTING POLICIES

The consolidated financial statements set out in the accountants' report in Appendix I to this prospectus have been prepared in accordance with Hong Kong Financial Reporting Standards. The preparation of the consolidated financial statements requires our management to make judgments, assumptions and estimates that affect the application of policies as well as the results of operations and financial position. We base the assumptions and estimates on historical experience and on various assumptions that we believe to be reasonable and which form the basis for making judgments about matters that are not readily apparent from other sources. Our management evaluates its estimates on an on-going basis. Actual results may differ from those estimates as facts, circumstances and

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conditions change. The significant accounting policies are set forth in note 3 to the accountants' report in Appendix I to this prospectus. We believe that the following critical accounting policies involve the most significant judgments and estimates used in the preparation of the consolidated financial statements.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold and services provided in the normal course of business, net of discounts and sales related taxes.

Revenue from sales of goods is recognised when goods are delivered and title has passed.

Revenue from construction contracts is recognised using the percentage of completion method by reference to the value of work carried out during the year/period as determined by progress verification certificate.

Rental income, including rental invoiced in advance from investment properties let under operating leases, is recognised on a straight line basis over the relevant lease terms.

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

Property, plant and equipment

Property, plant and equipment, including buildings held for use in production or supply of goods or services, or for administrative purposes are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of items of property, plant and equipment over their estimated useful lives and after taking into account of their estimated residual value, using the straight line method.

If an item of property, plant and equipment becomes an investment property because its use has changed as evidenced by end of owner-occupation, any difference between the carrying amount and the fair value of that item at the date of transfer is recognised in other comprehensive income and accumulated in property revaluation reserve. On the subsequent sale or retirement of the asset, the relevant revaluation reserve will be transferred directly to accumulated profits.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in profit or loss in the period in which the item is derecognised.

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Investment properties

Investment properties are properties held to earn rentals and/or capital appreciation.

On initial recognition, investment properties are measured at cost, including any directly attributable expenditure. Subsequent to initial recognition, investment properties are measured at their fair values using the fair value model based on the valuation carried out by an independent property valuer. Gains or losses arising from changes in the fair value of investment property are included in profit or loss for the period in which they arise.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposals. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the profit or loss in the period in which the item is derecognised.

Construction contracts

Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the end of the reporting period, as measured by progress verification certificate. Variations in contract work, claims and incentive payments are included to the extent that the amount can be measured reliably and its receipt is considered probable.

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred that it is probable will be recoverable. Contract costs are recognised as expenses in the period in which they are incurred.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is shown as amounts due from customers for contract work. For contracts where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is shown as amounts due to customers for contract work. Amounts received before the related work is performed are included in the consolidated statement of financial position, as a liability, as advances from customers. Amounts billed for work performed but not yet paid by the customer are included in the consolidated statement of financial position under trade and other receivables.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted average method.

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Impairment

At the end of the reporting period, our Group reviews the carrying amounts of its assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

DESCRIPTION OF SELECTED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME LINE ITEMS

Turnover

We generate our turnover primarily from the manufacture, sale and provision of maintenance, overhaul and modification services in respect of catalogued special-purpose tobacco machinery products, namely casing and flavouring system, PF system, PP system, and related components and devices not listed in all of the Tobacco Machinery Documents as well as non catalogued ancillary tobacco machinery products which mainly include dedusting systems and swelling agent delivery systems in the PRC.

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The following table sets forth a breakdown of our turnover by project category during the Track Record Period:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Catalogued special-purpose tobacco machinery projects								
Sales of tobacco machinery and parts/components/devices (<i>Note i</i>)								
Casing and flavouring systems	37,873	52.2	48,097	52.5	16,982	66.5	55,237	85.4
PF systems	10,545	14.5	13,790	15.0	5,215	20.4	936	1.5
PP systems	4,858	6.7	2,381	2.6	–	–	–	–
	<u>53,276</u>	<u>73.4</u>	<u>64,268</u>	<u>70.1</u>	<u>22,197</u>	<u>86.9</u>	<u>56,173</u>	<u>86.9</u>
Provision of maintenance, overhaul and modification services								
Casing and flavouring systems	11,288	15.5	13,091	14.3	769	3.0	2,137	3.3
PF systems	1,854	2.6	4,015	4.4	1,192	4.7	1,540	2.4
PP systems	805	1.1	6,095	6.6	510	2.0	273	0.4
	<u>13,947</u>	<u>19.2</u>	<u>23,201</u>	<u>25.3</u>	<u>2,471</u>	<u>9.7</u>	<u>3,950</u>	<u>6.1</u>
Sub-total								
Casing and flavouring systems	49,161	67.7	61,188	66.8	17,751	69.5	57,374	88.7
PF systems	12,399	17.1	17,805	19.4	6,407	25.1	2,476	3.9
PP systems	5,663	7.8	8,476	9.2	510	2.0	273	0.4
	<u>67,223</u>	<u>92.6</u>	<u>87,469</u>	<u>95.4</u>	<u>24,668</u>	<u>96.6</u>	<u>60,123</u>	<u>93.0</u>
Other projects and products								
Sales of non-catalogued ancillary tobacco machinery (<i>Note ii</i>)	1,636	2.2	2,125	2.3	–	–	2,286	3.5
Provision of maintenance, overhaul and modification services	3,757	5.2	498	0.5	870	3.4	–	–
Sales of hot stamped foil products	–	–	1,621	1.8	–	–	2,242	3.5
	<u>5,393</u>	<u>7.4</u>	<u>4,244</u>	<u>4.6</u>	<u>870</u>	<u>3.4</u>	<u>4,528</u>	<u>7.0</u>
Sub-total								
Casing and flavouring systems	49,161	67.7	61,188	66.8	17,751	69.5	57,374	88.7
PF systems	12,399	17.1	17,805	19.4	6,407	25.1	2,476	3.9
PP systems	5,663	7.8	8,476	9.2	510	2.0	273	0.4
	<u>67,223</u>	<u>92.6</u>	<u>87,469</u>	<u>95.4</u>	<u>24,668</u>	<u>96.6</u>	<u>60,123</u>	<u>93.0</u>
Total	<u><u>72,616</u></u>	<u><u>100.0</u></u>	<u><u>91,713</u></u>	<u><u>100.0</u></u>	<u><u>25,538</u></u>	<u><u>100.0</u></u>	<u><u>64,651</u></u>	<u><u>100.0</u></u>

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- Notes:* (i) Turnover of catalogued special-purpose tobacco machinery projects contracted with CTMC amounted to approximately HK\$53,208,000, HK\$60,589,000 and HK\$21,893,000, representing approximately 73.3%, 66.1% and 33.9% of our total turnover during the Track Record Period. Turnover generated from catalogued special-purpose tobacco machinery projects also includes that derived from sales of parts and sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents but form integral parts of the customised systems and are not contracted with CTMC, which amounted to approximately HK\$68,000, HK\$3,679,000 and HK\$34,280,000, representing 0.1%, 4.0 % and 53.0% of our total turnover respectively during the Track Record Period. Despite the separate sale and purchase agreement, as these components and/or devices were included in the technical specification of the corresponding catalogued special-purpose tobacco machinery projects and cannot function separately and independently from the catalogued special-purpose tobacco machinery system, the revenue derived from the sales of these items is classified under the relevant category of catalogued special-purpose tobacco machinery projects. The significant increase in the sales of these components and/or devices during the six months ended 30 June 2011 was mainly attributable to substantial turnover recognised from the customised casing and flavouring system with movable tanks project with our customer in Kunming during the period as further discussed below.
- (ii) Non-catalogued ancillary tobacco machinery products mainly comprised dedusting systems and swelling agent delivery systems.

During the Track Record Period, our turnover generated from sales of tobacco machinery amounted to approximately HK\$54,912,000, HK\$66,393,000 and HK\$58,459,000 respectively, while our turnover generated from the provision of maintenance, overhaul and modification services amounted to approximately HK\$17,704,000, HK\$23,699,000 and HK\$3,950,000 respectively. The significant decrease in our turnover derived from the provision of maintenance, overhaul and modification services during the six months ended 30 June 2011 was primarily attributable to (i) the decline in the number of provision of services contracts from which we derived revenue from 23 in 2009 and 28 in 2010 to 8 during the six months ended 30 June 2011; and (ii) the decrease in the average contract value mainly due to the decrease in the scope of the services provided as well as the complexity of the projects. As of 30 June 2011, there were 18 provision of services contracts with an aggregate contract value of approximately RMB7,038,000 still in progress and expected to be completed by the end of 2011. Our Directors are of the opinion that our Group is subject to variance in turnover mix due to its business being conducted on a project basis and such decrease was not due to seasonality.

In December 2010, we commenced to supply hot stamped foil used in cigarette packaging. The turnover derived from the sale of hot stamped foil was approximately HK\$1,621,000 for the year ended 31 December 2010, representing approximately 1.8% of our turnover for the year. The turnover derived from the sale of hot stamped foil amounted to approximately HK\$2,242,000 for the six months ended 30 June 2011, representing approximately 3.5% of our turnover for the period.

Our turnover generated from construction contracts of casing and flavouring systems is recognised using the percentage of completion method by reference to the value of work carried out during the year/period as determined by progress verification certificate. In general, the stage of completion of the casing and flavouring systems varies between contracts and is agreed with the end customers on a project by project basis with reference to, among others, the delivery, installation and testing of the systems. Our casing and flavouring system is a custom-made automated system designed for the purpose

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of creating the signature taste of cigarettes according to the unique recipes of individual cigarette brands. Hence, each cigarette manufacturer has its own specifications and requirements for the casing and flavouring system, varying from the number of tanks, the overall frame structure and the devices equipped with the system itself. Our end customers are capable of specifying the major structural elements of the system design, which are then concluded in the technical agreement signed between the end customer and our Group. Accordingly, under the interpretation of the relevant accounting standard applicable to the accounting period concerned, the sale of casing and flavouring systems is classified as revenue from construction contracts and recognised using percentage of completion method. Turnover from sales of all other products is classified as revenue from sales of goods as our customers or end customers specify minor variations to our basic design, such as the number of pipes and the layout of the piping system for our PF system, and the layout of the conveyor belts for our PP system. Turnover from all other products represents gross invoiced sales, net of discounts and value-added tax.

Our turnover generated from the sales of catalogued special-purpose tobacco machinery projects included that derived from sales of parts and sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents but form integral parts of the customised systems and are not contracted with CTMC, which amounted to approximately HK\$68,000, HK\$3,679,000 and HK\$34,280,000 respectively during the Track Record Period. The significant increase in the sales of these components and/or devices during the six months ended 30 June 2011 was mainly attributable to substantial turnover recognised from the customised casing and flavouring system with movable tanks project with our customer in Kunming during the period. As the first of its kind system built by our Group, the customisation of the said casing and flavouring system required the installation of certain components and devices which are not listed in all of the Tobacco Machinery Documents to meet our customer's specifications. Due to the larger scale, more customisation requests and higher degree of complexity of the customised system, the contract value for our supply of these components and devices accounted for a significant portion of the project's aggregate contract value of approximately RMB79,238,000, thus leading to a high turnover attributable to the sales of parts and sales of components and/or devices which are not listed in all of the Tobacco Machinery Documents during the period. No revenue was derived from this contract during the year ended 31 December 2010 as the first stage of this contract was not completed until the six-month period ended 30 June 2011.

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Cost of sales

The following table sets forth our cost of sales by project category during the Track Record Period:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Catalogued special-purpose tobacco machinery projects								
Casing and flavouring systems	32,519	73.6	38,781	75.9	12,973	82.1	40,031	91.4
PF systems	4,565	10.3	6,099	11.9	2,165	13.7	1,045	2.4
PP systems	3,924	8.9	3,703	7.3	109	0.7	154	0.4
	<u>41,008</u>	<u>92.8</u>	<u>48,583</u>	<u>95.1</u>	<u>15,247</u>	<u>96.5</u>	<u>41,230</u>	<u>94.2</u>
Non-catalogued ancillary tobacco machinery projects and other products								
	<u>3,187</u>	<u>7.2</u>	<u>2,516</u>	<u>4.9</u>	<u>553</u>	<u>3.5</u>	<u>2,546</u>	<u>5.8</u>
Total	<u><u>44,195</u></u>	<u><u>100.0</u></u>	<u><u>51,099</u></u>	<u><u>100.0</u></u>	<u><u>15,800</u></u>	<u><u>100.0</u></u>	<u><u>43,776</u></u>	<u><u>100.0</u></u>

The following table sets forth the components of our cost of sales and the percentage breakdown of total cost of sales during the Track Record Period:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Raw materials, parts and components								
Specialised metallic items	19,271	43.6	22,004	43.0	6,443	40.8	24,826	56.7
Counter modules	3,463	7.8	6,937	13.6	4,446	28.1	1,301	3.0
Steel plates and pipes	2,974	6.7	4,333	8.5	842	5.3	2,442	5.6
Electronic devices	2,156	4.9	4,294	8.4	676	4.3	2,397	5.4
Instruments and meters	8,865	20.1	3,194	6.2	391	2.5	2,451	5.6
Others	1,539	3.5	3,561	7.0	515	3.3	5,869	13.4
	<u>38,268</u>	<u>86.6</u>	<u>44,323</u>	<u>86.7</u>	<u>13,313</u>	<u>84.3</u>	<u>39,286</u>	<u>89.7</u>
Manufacturing costs	1,676	3.8	1,715	3.4	340	2.1	1,059	2.4
Direct labour costs	1,163	2.6	1,338	2.6	315	2.0	696	1.6
Subcontracting charges	1,024	2.3	1,345	2.6	590	3.7	912	2.1
Others	2,064	4.7	2,378	4.7	1,242	7.9	1,823	4.2
Total	<u><u>44,195</u></u>	<u><u>100.0</u></u>	<u><u>51,099</u></u>	<u><u>100.0</u></u>	<u><u>15,800</u></u>	<u><u>100.0</u></u>	<u><u>43,776</u></u>	<u><u>100.0</u></u>

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Our cost of sales mainly consists of raw material, part and component costs, manufacturing costs, direct labour costs and subcontracting charges. Raw material, part and component costs mainly consist of our cost for the purchase of specialised metallic items, counter modules, steel plates and pipes, electronic devices as well as instruments and meters. We purchase our raw materials, parts and components based on the requirements of the projects being undertaken as our business is project based and our products are highly customised. Manufacturing costs primarily include consumables, maintenance expenses and depreciation relating primarily to property, plant and equipment we own. Direct labour costs mainly represent compensation and benefits we offer to manufacturing employees. Subcontracting charges represent outsourced processing fees paid to third parties.

Raw material, part and component costs, manufacturing costs, direct labour costs as well as subcontracting charges as a percentage of cost of sales remained stable during the Track Record Period. We use various raw materials, parts and components in our production process, including primarily specialised metallic items, which is the largest component of our raw material, part and component costs, accounting for approximately 43.6%, 43.0% and 56.7% of our total costs of sales respectively and approximately 50.4%, 49.6% and 63.2% of our raw material, part and component costs for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. The increase in specialised metallic items as a percentage of our total cost of sales for the six months ended 30 June 2011 was mainly due to more specialised metallic items utilised for the casing and flavouring system project for the cigarette manufacturer in Kunming during the period.

Gross profit and gross profit margin

The following table sets out the breakdown of our Group's gross profit and gross profit margin by project category during the Track Record Period:

	Year ended 31 December						Six months ended 30 June					
	2009			2010			2010			2011		
	Percentage		Gross profit	Percentage		Gross profit	Percentage		Gross profit	Percentage		Gross profit
	Gross profit margin	of total gross profit		Gross profit margin	of total gross profit		Gross profit margin	of total gross profit		Gross profit margin	of total gross profit	
HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%	
Catalogued special-purpose tobacco machinery projects												
Casing and flavouring systems	16,642	33.9	58.6	22,407	36.6	55.2	4,778	26.9	49.1	17,343	30.2	83.1
PF systems	7,834	63.2	27.6	11,706	65.7	28.8	4,242	66.2	43.6	1,431	57.8	6.8
PP systems	1,739	30.7	6.1	4,773	56.3	11.8	401	78.6	4.1	119	43.4	0.6
	<u>26,215</u>	<u>39.0</u>	<u>92.3</u>	<u>38,886</u>	<u>44.5</u>	<u>95.8</u>	<u>9,421</u>	<u>38.2</u>	<u>96.8</u>	<u>18,893</u>	<u>31.4</u>	<u>90.5</u>
Non-catalogued ancillary tobacco machinery projects and other products												
	<u>2,206</u>	<u>40.9</u>	<u>7.7</u>	<u>1,728</u>	<u>40.7</u>	<u>4.2</u>	<u>317</u>	<u>36.4</u>	<u>3.2</u>	<u>1,982</u>	<u>43.8</u>	<u>9.5</u>
Total	<u><u>28,421</u></u>	<u><u>39.1</u></u>	<u><u>100.0</u></u>	<u><u>40,614</u></u>	<u><u>44.3</u></u>	<u><u>100.0</u></u>	<u><u>9,738</u></u>	<u><u>38.1</u></u>	<u><u>100.0</u></u>	<u><u>20,875</u></u>	<u><u>32.3</u></u>	<u><u>100.0</u></u>

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Our gross profit for each of the two years ended 31 December 2010 and the six months ended 30 June 2011 was approximately HK\$28,421,000, HK\$40,614,000 and HK\$20,875,000 respectively. Our gross profit margin increased from approximately 39.1% in 2009 to approximately 44.3% in 2010 primarily reflecting the increases in gross profit margin in all of our catalogued special-purpose tobacco machinery products. Our gross profit margin decreased to approximately 32.3% in the first six months of 2011 due to the decrease in gross profit margin for our casing and flavouring systems as well as the decrease in turnover from our PF systems and PP systems which generated higher gross profit margins than our casing and flavouring systems. During the Track Record Period, we generated a higher gross profit margin from our PF systems than that from our casing and flavouring systems as well as PP systems. Our Directors believe that the prices of PF systems were originally set by STMA with reference to the selling prices of imported PF systems. With the localisation of production and savings in transportation costs and custom duties, we are able to enjoy a higher gross margin for our PF systems than other products.

Other income

During the Track Record Period, other income mainly comprised sales of materials, bank interest income, rental income from related companies and refund from local tax authority. We enjoy a preferential treatment of tax refund equivalent to 16% of the PRC enterprise income tax paid in prior year and 12.5% of the excess of the value-added tax paid by Baoying Renheng in prior year over the value-added tax paid by Baoying Radio Factory in 2000. For further details, please refer to the paragraph headed "Taxation" under this section in this prospectus.

Other gains and losses

Our other gains and losses mainly related to gain on fair value changes of investment properties and loss on disposal of property, plant and equipment.

Selling and distribution costs

The following table sets out the breakdown of our Group's selling and distribution costs and the components as a percentage of total selling and distribution costs during the Track Record Period:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Selling and distribution costs								
Entertainment	3,889	42.9	2,289	26.0	1,086	25.9	3,826	54.8
Handling fee	1,808	19.9	3,201	36.3	1,225	29.2	136	1.9
Travelling	839	9.3	931	10.5	241	5.8	500	7.2
Transportation	662	7.3	688	7.8	332	7.9	852	12.2
Office expenses	392	4.3	164	1.9	104	2.5	49	0.7
Staff costs	994	11.0	1,367	15.5	1,131	27.0	1,462	20.9
Others	480	5.3	177	2.0	70	1.7	160	2.3
Total	<u>9,064</u>	<u>100.0</u>	<u>8,817</u>	<u>100.0</u>	<u>4,189</u>	<u>100.0</u>	<u>6,985</u>	<u>100.0</u>

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Our selling and distribution costs mainly include entertainment expenses, handling fee, travelling expenses, staff costs, transportation costs and office expenses. Selling and distribution costs represented 12.5%, 9.6% and 10.8% of our turnover for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. The entertainment expenses and handling fee accounted for significant portions of our selling and distribution costs during the Track Record Period, being 42.9% and 19.9% for the year ended 31 December 2009 respectively, 26.0% and 36.3% for the year ended 31 December 2010 respectively and 54.8% and 1.9% for the six months ended 30 June 2011 respectively. The increase in entertainment expenses as a percentage of our selling and distribution costs for the six months ended 30 June 2011 was mainly due to the visits our sales and marketing staff made to our customers to explore potential business opportunities during the period. Handling fee represents the amount payable to CTMC based on the sales of catalogued special-purpose machinery products to our end customers. Since the incorporation of Baoying Renheng and up to the Latest Practicable Date, the handling fee for each type of catalogued special-purpose machinery products was charged by CTMC at 3% of the value of the contracts entered into between our Group and CTMC. The amounts were not paid separately by us, but were deducted by CTMC directly from its progress payments made to our Group. In view of the current settlement arrangements amongst CTMC, our Group and the end customers in respect of the procurements of catalogued special-purpose machinery products as set out in the paragraph headed “Business model” in the section headed “Business” in this prospectus, our Directors believe that we are still liable to the handling fee payable to CTMC if an end customer defaults on its payment to CTMC for the purchase of our products. During the Track Record Period and up to the Latest Practicable Date, we did not receive any notice from CTMC requesting settlement of the handling fee prior to receiving payment from CTMC in relation to the relevant contract. As at 31 December 2009 and 2010 and 30 June 2011, we had no handling fee payable to CTMC as the trade receivables due from CTMC had been fully settled.

Staff costs mainly comprise salary, bonus and welfare expenses for our employees involved in selling and distribution activities. We provide our sales and marketing staff with a sales bonus ranging between RMB1,000 to RMB4,000 for sale of a set of casing and flavouring system, dedusting system or swelling agent delivery system with a contract value not exceeding RMB2,000,000. A year end discretionary bonus will be paid to our sales and marketing staff for sale of a set of casing and flavouring system, dedusting system or swelling agent delivery system with a contract value above RMB2,000,000 after taking into account various factors including, among others, the aggregate value of projects completed during the year, total selling and distribution costs incurred, sales proceeds received by our Group, profit margin of the contracts secured and the general performance of the sales and marketing staff. As regards our PF system and PP system projects, an incentive payment of RMB3,000 and RMB8,000 per set will be made to our sales and marketing staff respectively for sales achieved by each of them.

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Administrative expenses

The following table sets out the breakdown of our Group's administrative expenses during the Track Record Period:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	HK\$'000	%	HK\$'000	%	HK\$'000	%	HK\$'000	%
Administrative expenses								
Staff costs	2,669	43.2	3,479	46.7	1,459	44.7	2,300	38.6
Audit fee	610	9.9	285	3.8	159	4.9	263	4.4
Other taxes	454	7.4	522	7.0	516	15.8	940	15.8
Travelling	309	5.0	553	7.4	214	6.5	231	3.9
Entertainment	166	2.7	264	3.6	152	4.6	301	5.0
Office expenses	211	3.4	271	3.6	115	3.5	156	2.6
Repairs and maintenance	174	2.8	456	6.1	182	5.6	86	1.4
Research and development	246	4.0	394	5.3	5	0.2	717	12.0
Legal and professional fees	27	0.4	–	–	–	–	78	1.3
Depreciation	515	8.3	494	6.6	238	7.3	314	5.3
Rental expenses	–	–	–	–	–	–	102	1.7
Others	801	12.9	738	9.9	227	6.9	475	8.0
Total	6,182	100.0	7,456	100.0	3,267	100.0	5,963	100.0

Administrative expenses mainly represent staff costs, audit fee, travelling expenses, entertainment expenses, office expenses, repair and maintenance, research and development costs, legal and professional fees and depreciation. Administrative expenses represented 8.5%, 8.1% and 9.2% of our turnover for the two years ended 31 December 2010 and the six months ended 30 June 2011 respectively. Staff costs mainly comprise salary, bonus and welfare expenses. Our staff costs accounted for the largest component of our administrative expenses for each of the two years ended 31 December 2009 and 2010, representing approximately 43.2% and 46.7% of our Group's administrative expenses. The staff costs for the six months ended 30 June 2011 amounted to approximately HK\$2,300,000, representing approximately 38.6% of our administrative expenses for the period and an increase by 57.6% as compared to the corresponding period in 2010, which was mainly attributable to the bonus paid to our staff during the period. The audit fee decreased by approximately HK\$325,000 from approximately HK\$610,000 for the year ended 31 December 2009 to approximately HK\$285,000 for the year ended 31 December 2010 mainly because the audit fees charged in 2009 comprised fees for the two years ended 31 December 2008 and 2009, while the audit fee charged in 2010 comprised audit fee for the year ended 31 December 2010. The audit fee charged for the six months ended 30 June 2011 amounted to approximately HK\$263,000, representing an increase of approximately 65.4% as compared to the corresponding period in 2010, which primarily due to the increase in audit fee in relation to our Listing.

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Taxation

Our subsidiary incorporated in the PRC is subject to PRC enterprise income tax and value-added tax. As advised by the PRC Legal Advisers, in accordance with the relevant income tax laws and regulations of the PRC, Baoying Renheng was exempted from enterprise income tax for two years commencing from 2002, and was entitled to a 50% reduction in its enterprise income tax for the subsequent three years. Therefore, from 1 January 2004 to 31 December 2006, the applicable enterprise income tax rate for Baoying Renheng was 15%. With effect from 1 January 2008, Baoying Renheng is subject to an enterprise income tax rate of 25% pursuant to the Law of the PRC on Enterprise Income Tax and Implementation Legislation. Baoying Renheng enjoyed the preferential treatments granted by the People's Government of Baoying pursuant to which (i) Baoying Renheng would receive a refund of 50% of enterprise income tax in respect to the portion received by the People's Government of Baoying, which would be equivalent to 16% of the total enterprise income tax paid for the respective years, for a period of 5 years from 1 January 2007 to 31 December 2011; and (ii) Baoying Renheng would receive a 12.5% refund of the excess of the value-added tax paid by Baoying Renheng in prior year over the value-added tax paid by Baoying Radio Factory in 2000, for an indefinite period of time.

OUR RESULTS OF OPERATIONS

Summary of results of operations

	Year ended 31 December		Six months ended 30 June	
	2009	2010	2010	2011
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
			(unaudited)	
Turnover	72,616	91,713	25,538	64,651
Cost of sales	(44,195)	(51,099)	(15,800)	(43,776)
Gross profit	28,421	40,614	9,738	20,875
Other income	3,877	4,279	2,154	1,038
Other gains and losses	34	713	510	(14)
Selling and distribution costs	(9,064)	(8,817)	(4,189)	(6,985)
Administrative expenses	(6,182)	(7,456)	(3,267)	(5,963)
Listing expenses	–	(1,595)	–	(2,225)
Interest on bank loans wholly repayable within five years	(353)	–	–	–
Profit before taxation	16,733	27,738	4,946	6,726
Taxation	(5,748)	(7,805)	(1,512)	(3,108)
Profit for the year/period	10,985	19,933	3,434	3,618
Other comprehensive income:				
Exchange differences arising on translation	592	2,775	622	2,235
Total comprehensive income for the year/period	<u>11,577</u>	<u>22,708</u>	<u>4,056</u>	<u>5,853</u>

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Turnover

A breakdown of our turnover during the Track Record Period is set out as follows:

	Year ended 31 December				Six months ended 30 June			
	2009		2010		2010		2011	
	Number of contracts	Turnover HK\$'000	Number of contracts	Turnover HK\$'000	Number of contracts	Turnover HK\$'000	Number of contracts	Turnover HK\$'000
Catalogued special-purpose tobacco machinery projects								
Casing and flavouring systems	20	49,161	22	61,188	4	17,751	9	57,374
PF systems	18	12,399	16	17,805	4	6,407	6	2,476
PP systems	4	5,663	8	8,476	1	510	1	273
	<u>42</u>	<u>67,223</u>	<u>46</u>	<u>87,469</u>	<u>9</u>	<u>24,668</u>	<u>16</u>	<u>60,123</u>
Non-catalogued ancillary tobacco machinery projects and other products								
	<u>8</u>	<u>5,393</u>	<u>5</u>	<u>4,244</u>	<u>1</u>	<u>870</u>	<u>8</u>	<u>4,528</u>
Total	<u>50</u>	<u>72,616</u>	<u>51</u>	<u>91,713</u>	<u>10</u>	<u>25,538</u>	<u>24</u>	<u>64,651</u>

Year ended 31 December 2010 compared to year ended 31 December 2009

Our turnover increased by approximately 26.3% or HK\$19,097,000 from approximately HK\$72,616,000 for the year ended 31 December 2009 to approximately HK\$91,713,000 for the year ended 31 December 2010. The increase was mainly attributable to increases in turnover from our catalogued special-purpose tobacco machinery products.

Turnover derived from our casing and flavouring systems increased by approximately 24.5% or HK\$12,027,000 from approximately HK\$49,161,000 for the year ended 31 December 2009 to approximately HK\$61,188,000 for the year ended 31 December 2010, which was primarily attributable to a general increase in the individual contract value of the casing and flavouring system projects we undertook in 2010. As set out in the paragraph headed “Business model” in the section headed “Business” in this prospectus, the number of casing and flavouring system contracts with contract value above RMB5 million we completed during each of the two years ended 31 December 2009 and 2010 was three and four respectively, with the average contract value amounting to approximately RMB8,610,000 and RMB11,429,250 respectively. In addition, we recognised turnover of approximately HK\$8,723,000 from a casing and flavouring system project for a cigarette manufacturer in Kunming with the contract value of approximately RMB29,423,000 in 2010, based on the percentage of completion method by reference to the value of work carried out. The increase in the average contract value was mainly due to the increase in the scale of the project as well as the design requirements of the products provided.

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Turnover derived from our PF systems increased by approximately 43.6% or HK\$5,406,000 from approximately HK\$12,399,000 for the year ended 31 December 2009 to approximately HK\$17,805,000 for the year ended 31 December 2010. The increase in turnover was mainly attributable to the increase in the contract value of our PF systems projects undertaken in 2010. Despite the decline in the number of PF system projects undertaken from 18 in 2009 to 16 in 2010, we experienced an increase in the turnover generated from PF system projects in 2010. In addition, the contract value of 7 out of 16 PF system projects completed during 2010 was above RMB1 million whilst in 2009, only 4 out of 18 projects completed with contract value of above RMB1 million.

Turnover derived from our PP systems increased by approximately 49.7% or HK\$2,813,000 from approximately HK\$5,663,000 for the year ended 31 December 2009 to approximately HK\$8,476,000 for the year ended 31 December 2010. The increase in turnover was mainly attributable to the increase in the number of PP system repair and maintenance projects completed from 2 in 2009 to 7 in 2010. The total turnover generated from PP system repair and maintenance projects increased from approximately HK\$806,000 for the year ended 31 December 2009 to approximately HK\$6,094,000 for the year ended 31 December 2010.

Our non-catalogued ancillary tobacco machinery products mainly comprised dedusting systems and swelling agent delivery systems. The turnover derived from non-catalogued ancillary tobacco machinery products decreased by approximately 21.3% or approximately HK\$1,149,000 from approximately HK\$5,393,000 for the year ended 31 December 2009 to approximately HK\$4,244,000 for the year ended 31 December 2010. The decrease was primarily due to the reduction in the number of non-catalogued ancillary tobacco machinery product projects in 2010. In December 2010, we commenced to supply hot stamped foil used in cigarette packaging. The turnover derived from the sale of hot stamped foil was approximately HK\$1,621,000 for the year ended 31 December 2010.

Six months ended 30 June 2011 compared to six months ended 30 June 2010

Our turnover increased by approximately 153.2% or HK\$39,113,000 from approximately HK\$25,538,000 for the six months ended 30 June 2010 to approximately HK\$64,651,000 for the six months ended 30 June 2011. The increase was mainly attributable to substantial turnover recognised from our customised casing and flavouring system with movable tanks to a cigarette manufacturer in Kunming for the six months ended 30 June 2011 which had an aggregate contract value of approximately RMB79,238,000.

Turnover derived from our casing and flavouring systems increased by approximately 223.2% or HK\$39,623,000 from approximately HK\$17,751,000 for the six months ended 30 June 2010 to approximately HK\$57,374,000 for the six months ended 30 June 2011, which was primarily attributable to recognition of turnover of approximately HK\$51,369,000 from our customised casing and flavouring system project for the cigarette manufacturer in Kunming as mentioned above. During the corresponding period in 2010, we derived revenue from four casing and flavouring system contracts with lower aggregate contract value of approximately RMB18,164,000.

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Turnover derived from our PF systems decreased by approximately 61.4% from approximately HK\$6,407,000 for the six months ended 30 June 2010 to approximately HK\$2,476,000 for the six months ended 30 June 2011. The decrease was mainly attributable to the decrease in average contract value of our projects completed during the period. Specifically, out of the 6 PF system projects completed for the six months ended 30 June 2011, we have completed only 1 PF system project with contract value exceeding RMB1 million, as compared to 2 projects completed out of 4 PF system projects completed for the six months ended 30 June 2010.

Turnover derived from our PP systems decreased by approximately 46.5% from approximately HK\$510,000 for the six months ended 30 June 2010 to approximately HK\$273,000 for the six months ended 30 June 2011, which was mainly attributable to the decrease in the contract value of our PP system project completed for the six months ended 30 June 2011.

Turnover derived from non-catalogued ancillary tobacco machinery increased by approximately HK\$3,658,000 from approximately HK\$870,000 for the six months ended 30 June 2010 to approximately HK\$4,528,000 for the six months ended 30 June 2011. It is mainly due to the sales of hot stamped foil of approximately HK\$2,242,000 and the sale of swelling agent delivery systems of approximately HK\$2,286,000 during the six months ended 30 June 2011.

Cost of sales

Year ended 31 December 2010 compared to year ended 31 December 2009

Our cost of sales increased by approximately 15.6% or HK\$6,904,000 from approximately HK\$44,195,000 for the year ended 31 December 2009 to approximately HK\$51,099,000 for the year ended 31 December 2010, which was mainly due to the increase in our turnover and the total number of projects undertaken during the year. Our raw material, part and component costs, manufacturing costs, direct labour costs as well as subcontracting charges as a percentage of total cost of sales remained stable during the Track Record Period.

Six months ended 30 June 2011 compared to six months ended 30 June 2010

Our cost of sales for the six months ended 30 June 2011 amounted to HK\$43,776,000, representing an increase of approximately 177.1% as compared to our cost of sales for the six months ended 30 June 2010. The significant increase was mainly attributable to those incurred for our casing and flavouring systems. During the six months ended 30 June 2011, the cost of sales for our casing and flavouring systems amounted to approximately HK\$40,031,000, representing approximately 91.4% of our total cost of sales and was in line with the proportion of turnover generated from our casing and flavouring systems during the period. During the period, we also sourced hot stamped foil of approximately HK\$1,445,000 for our sale of hot stamped foil products, which we commenced in December 2010. Our raw material, part and component costs as a percentage of the total cost of sales increased from 84.3% for the six months ended 30 June 2010 to 89.7% for the six months ended 30 June 2011, which was mainly due to higher costs associated with the components and devices sourced from independent suppliers for the aforementioned casing and flavouring system project for the cigarette manufacturer in Kunming during the period.

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Gross profit and gross profit margin

Year ended 31 December 2010 compared to year ended 31 December 2009

Our gross profit increased by approximately 42.9% or HK\$12,193,000 from approximately HK\$28,421,000 for the year ended 31 December 2009 to approximately HK\$40,614,000 for the year ended 31 December 2010. Our gross profit margin increased from approximately 39.1% for the year ended 31 December 2009 to approximately 44.3% for the year ended 31 December 2010. The increase was primarily caused by an increase in gross profit margin in our catalogued special-purpose tobacco machinery products which was in turn mainly due to the increase in the scale of our projects. The increase in our gross profit margin was also attributable to the increase in the contribution of turnover generated from our PF system projects, which are of higher gross profit margin and accounted for approximately 19.4% of the turnover of our Group for the year ended 31 December 2010.

The gross profit margin of casing and flavouring systems increased from approximately 33.9% in 2009 to approximately 36.6% in 2010. The lower gross profit margin recorded in 2009 was mainly attributable to a project with respect to the sale of casing and flavouring system to a cigarette manufacturer with a contract value of approximately RMB9.9 million and gross profit margin of approximately 7.9%. We set the project at a lower sales price in order to enhance our competitiveness in securing the contract with the relevant cigarette manufacturer who was a new customer in 2009.

The gross profit margin of PF systems increased from approximately 63.2% in 2009 to approximately 65.7% in 2010 mainly due to the increase in the gross profit generated from our PF system sales projects which were of higher gross profit margin than our PF system repair and maintenance projects. In 2009, we completed 11 system sales projects with aggregate gross profit of approximately HK\$6,353,000 and 7 repair and maintenance projects with aggregate gross profit of approximately HK\$1,018,000, representing gross profit margin of approximately 68.3% and approximately 62.3% respectively. In 2010, we completed 7 system sales projects with aggregate gross profit of approximately HK\$7,386,000 and 9 repair and maintenance projects with aggregate gross profit of approximately HK\$2,910,000, representing gross profit margin of approximately 70.7% and approximately 58.8% respectively.

The gross profit margin of PP systems increased from approximately 30.7% in 2009 to approximately 56.3% in 2010. The improvement in the gross profit margin was mainly attributable to the increase in the number of PP system repair and maintenance projects completed from 2 in 2009 to 7 in 2010. During the two years ended 31 December 2010, we generated a higher gross profit margin from our PP system repair and maintenance projects than that from our PP system sales projects. In 2009, we completed 2 system sales projects with aggregate gross profit of approximately HK\$1,273,000 and 2 repair and maintenance projects with aggregate gross profit of approximately HK\$326,000, representing gross profit margin of approximately 29.7% and approximately 45.9% respectively. In 2010, we completed 1 system sales project with gross profit of approximately HK\$946,000 and 7 repair and maintenance projects with aggregate gross profit of approximately HK\$3,232,000, representing gross profit margin of approximately 45.9% and approximately 61.3% respectively.

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Our non-catalogued ancillary tobacco machinery products mainly comprised dedusting systems and swelling agent delivery systems. The gross profit margin of our non-catalogued ancillary tobacco machinery products remained relatively stable at around 41% during the Track Record Period. Nevertheless, the gross profit margin of dedusting systems increased from approximately 40.2% in 2009 to 52.0% in 2010, while the gross profit margin of swelling agent delivery systems decreased from approximately 58.6% in 2009 to 52.7% in 2010. The fluctuations were mainly due to the number of projects undertaken by us during the Track Record Period. In 2009, we undertook 7 dedusting system projects with gross profit margin ranging from 17.1% to 67.4%, while in 2010, we undertook only one dedusting system project with gross profit margin of approximately 52.0%. As regards our swelling agent delivery systems, we undertook only 1 project in 2009 with gross profit margin of approximately 58.6% and 3 projects in 2010 with gross profit margin ranging from 51.0% to 57.1%. In addition, we commenced to supply hot stamped foil used in cigarette packaging in December 2010. The gross profit margin relating to the sale of hot stamped foil was approximately 29.1% for the year ended 31 December 2010.

Six months ended 30 June 2011 compared to six months ended 30 June 2010

Our gross profit for the six months ended 30 June 2011 amounted to HK\$20,875,000, representing an increase of 114.4% as compared to the gross profit of HK\$9,738,000 for the six months ended 30 June 2010. Notwithstanding the increase in gross profit, our gross profit margin for the six months ended 30 June 2011 decreased to 32.3%, as compared to the gross profit margin of 38.1% for the corresponding period in 2010 and 44.3% for the year ended 31 December 2010. Despite the higher gross profit margin for our casing and flavouring system for the six months ended 30 June 2011 as compared to that for the corresponding period in 2010, the decrease in our gross profit margin in 2011 was mainly attributable to the decrease in turnover from our PF systems and PP systems which generated higher gross profit margins than our casing and flavouring systems. Furthermore, as compared to the year ended 31 December 2010, the decrease in our gross profit margin for the six months ended 30 June 2011 was also attributable to the decrease in gross profit margin of our casing and flavouring system as further discussed below.

The gross profit margin of casing and flavouring systems was 30.2% for the six months ended 30 June 2011, which was higher than that of 26.9% for the corresponding period in 2010 but was lower than that of 36.6% for the year ended 31 December 2010. The decrease in our gross profit margin in the first half of 2011 as compared to the full year of 2010 was mainly attributable to the project contracted in April 2010 with an aggregate contract value of approximately RMB79,238,000, in which we contracted to supply a customised casing and flavouring system with movable tanks for a cigarette manufacturer in Kunming. An aggregate turnover of approximately HK\$51,369,000 was recognised in relation to this project for the six months ended 30 June 2011 and the entire project is expected to be completed in November 2011. As this customised casing and flavouring system with movable tanks was the first of its kind that we built and its technical viability could not be foreseen with certainty, our Group has accepted a low mark up relative to the expected costs in respect of the components and devices when deciding the aggregate contract amount charged to the end customer based on mutual agreement, resulting in a lower gross profit margin for this project and thus the lower gross profit margin for our casing and flavouring systems for the period.

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The gross profit margin of our PF systems was 57.8% for the six months ended 30 June 2011, which was lower than that of 66.2% for the corresponding period in 2010 and that of 65.7% for the year ended 31 December 2010. The gross profit margin for our PF systems decreased slightly for the six months ended 30 June 2011 as a higher percentage of turnover from our PF systems was derived from the modification contracts of PF systems completed during the period, which had a lower gross profit margin than our PF system sales projects. The modification contracts usually carry lower contract values and their respective gross profit margins may fluctuate based on the nature of modification works performed for our customers. Furthermore, additional cost of sales of approximately HK\$363,000 in relation to PF system projects completed in previous years was recognised as minor fine-tunings were required within the systems' warranty period. This was higher than the corresponding additional cost of sales incurred for previously completed projects, which amounted to approximately HK\$98,000 for the six months ended 30 June 2010.

The gross profit margin of our PP systems was 43.4% for the six months ended 30 June 2011, which was lower than that of 78.6% for the corresponding period in 2010 and that of 56.3% for the year ended 31 December 2010. The lower gross profit margin for the six months ended 30 June 2011 was mainly due to the recognition of additional costs of sales of approximately HK\$95,000 in relation to PP system projects completed in previous years where minor fine-tunings were required within the systems' warranty period. Meanwhile, during the six months ended 30 June 2011, we completed only one project which involved the modification and maintenance works of PP system, which had comparable gross profit margin to our previous PP system projects.

During the six months ended 30 June 2011, the gross profit margin for the sales of parts and sales of components and devices which were not listed in all of the Tobacco Machinery Documents and were not contracted with CTMC but form integral parts of the customised systems was approximately 24.9%, whilst the gross profit margin for the sales of components and devices in respect of the customised casing and flavouring system with movable tanks for a cigarette manufacturer in Kunming was approximately 22.3%.

The gross profit margin of non-catalogued ancillary tobacco machinery products was 43.8% for the six months ended 30 June 2011, which was higher than that of 36.4% for the six months ended 30 June 2010 and that of 40.7% for the year ended 31 December 2010. The gross profit of approximately HK\$1,938,000 for the six months ended 30 June 2011 included the gross profit derived from our hot stamped foil of approximately HK\$798,000, representing a gross profit margin of approximately 35.6%. The increase in gross profit margin for the six month ended 30 June 2011 was mainly attributable to the two swelling agent delivery system projects which had gross profit margins of 51.7% and 56.7% respectively.

Other income

Year ended 31 December 2010 compared to year ended 31 December 2009

Other income increased slightly from approximately HK\$3,877,000 for the year ended 31 December 2009 to HK\$4,279,000 for the year ended 31 December 2010 primarily due to the increase in the amount of bank interest income and the tax refund from local tax authority.

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Six months ended 30 June 2011 compared to six months ended 30 June 2010

Other income decreased from HK\$2,154,000 for the six months ended 30 June 2010 to HK\$1,038,000 for the six months ended 30 June 2011 as our Group did not recognise any income from tax refund for the six months ended 30 June 2011 as our Group has not yet received the refund during the period.

Other gains and losses

Year ended 31 December 2010 compared to year ended 31 December 2009

Other gains and losses amounted to approximately HK\$713,000 for the year ended 31 December 2010, representing an increase of approximately HK\$679,000 from approximately HK\$34,000 for the year ended 31 December 2009 which was attributable to the gain on fair value changes of investment properties of approximately HK\$786,000.

Six months ended 30 June 2011 compared to six months ended 30 June 2010

Our Group recognised other losses of approximately HK\$14,000 for the six months ended 30 June 2011 as compared to other gains of approximately HK\$510,000 recognised for the six months ended 30 June 2010. The other losses for the six months ended 30 June 2011 were mainly attributable to the provision of allowance for doubtful debts of approximately HK\$288,000, partially offset by the gain on fair value changes of investment properties of approximately HK\$274,000.

Selling and distribution costs

Year ended 31 December 2010 compared to year ended 31 December 2009

Our selling and distribution costs decreased slightly by approximately HK\$247,000, or 2.7%, from approximately HK\$9,064,000 in 2009 to HK\$8,817,000 in 2010. Such decrease was primarily due to a decrease in entertainment expenses, partially offset by an increase in handling fee paid to CTMC associated with the increase in our turnover derived from catalogued special-purpose tobacco machinery products.

The decrease in entertainment expenses in 2010 was mainly due to the visit to a cigarette manufacturer in 2009 in order to obtain a project contract of approximately RMB29,423,000 in value.

Six months ended 30 June 2011 compared to six months ended 30 June 2010

Our selling and distribution costs increased from approximately HK\$4,189,000 for the six months ended 30 June 2010 to approximately HK\$6,985,000 for the six months ended 30 June 2011 primarily due to the increase in entertainment, travelling and transportation expenses resulting from our visits to various potential customers, and the increase in our staff costs for the period as more bonus was paid to our sales and marketing staff. Such increase was partially offset by the decrease in handling fee paid to CTMC.

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Administrative expenses

Year ended 31 December 2010 compared to year ended 31 December 2009

Our administrative expenses increased by approximately HK\$1,274,000, or 20.6%, from approximately HK\$6,182,000 in 2009 to HK\$7,456,000 in 2010. Such increase was primarily due to the increase in staff costs in line with our business growth.

Six months ended 30 June 2011 compared to six months ended 30 June 2010

Our administrative expenses increased from approximately HK\$3,267,000 for the six months ended 30 June 2010 to approximately HK\$5,963,000 for the six months ended 30 June 2011. Such increase was primarily due to the increase in staff costs, other taxes and research and development expenses during the period.

Interest on bank loans

The interest on bank loans wholly repayable within five years recorded approximately HK\$353,000 for the year ended 31 December 2009 but decreased to nil and nil for each of the year ended 31 December 2010 and the six months ended 30 June 2011 due to full settlement of all bank loans in the year 2009.

Taxation

Year ended 31 December 2010 compared to year ended 31 December 2009

Taxation amounted to approximately HK\$7,805,000 for the year ended 31 December 2010, representing an increase of approximately HK\$2,057,000 from approximately HK\$5,748,000 for the year ended 31 December 2009 mainly due to the increase in profit before taxation. Our effective tax rate, calculated as our Group's tax charge for the year divided by profit before taxation, for the year ended 31 December 2010 was approximately 28.1%, as compared to approximately 34.4% for the year ended 31 December 2009. The decline in the effective tax rate in 2010 is primarily attributable to the withholding tax on undistributed profits and the expenses not deductible for tax purposes in 2009.

Six months ended 30 June 2011 compared to six months ended 30 June 2010

Taxation amounted to approximately HK\$3,108,000 for the six months ended 30 June 2011, representing an increase of approximately HK\$1,596,000 from approximately HK\$1,512,000 for the six months ended 30 June 2010, which was in line with the increase in profit before taxation and our effective tax rate. Our effective tax rate increased from 30.6% for the six months ended 30 June 2010 to approximately 46.2% for the six months ended 30 June 2011 primarily attributable to the higher expenses not deductible for tax purposes incurred for the six months ended 30 June 2011.

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Profit for the year/period and net profit margin

As a result of the foregoing, our Group's profit for the year increased from approximately HK\$10,985,000 for the year ended 31 December 2009 to approximately HK\$19,933,000 for the year ended 31 December 2010, representing an increase of approximately 81.5%. Our net profit margin increased from approximately 15.1% for the year ended 31 December 2009 to approximately 21.7% for the year ended 31 December 2010.

Our Group's profit for the six months ended 30 June 2011 was approximately HK\$3,618,000, representing an increase of approximately 5.4% as compared to the profit of approximately HK\$3,434,000 for the six months ended 30 June 2010. Meanwhile, our net profit margin decreased from approximately 13.4% for the six months ended 30 June 2010 to approximately 5.6% for the six months ended 30 June 2011, which was in line with the decrease in gross profit margin, the recognition of listing expenses and the increase in our effective tax rate for the period as discussed above.

ANALYSIS ON CERTAIN SELECTED FINANCIAL RATIOS

Major financial ratios

	<i>Notes</i>	Year ended 31 December		Six months ended 30 June
		2009	2010	2011
Return on equity	<i>a</i>	15.4%	21.2%	3.6%
Return on assets	<i>b</i>	11.6%	13.0%	2.1%
		As at 31 December		As at 30 June
		2009	2010	2011
Current ratio	<i>c</i>	2.7	2.0	1.9
Quick ratio	<i>d</i>	1.7	1.7	1.6
Gearing ratio	<i>e</i>	24.5%	38.6%	41.4%

Notes:

- a. Return on equity is calculated based on the net profit for the year/period divided by the total equity as of the end of the corresponding year/period. The return of equity for the six months ended 30 June 2011 is not annualised and is presented herein for illustrative purpose only.
- b. Return on assets is calculated based on the net profit for the year/period divided by total assets as of the end of the corresponding year/period. The return on assets for the six months ended 30 June 2011 is not annualised and is presented herein for illustrative purpose only.
- c. Current ratio is calculated based on the current assets divided by current liabilities as of the end of the corresponding year/period.

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- d. Quick ratio is calculated based on the current assets less inventories as of the end of the corresponding year/period and then divided by the current liabilities as of the end of the corresponding year/period.
- e. Gearing ratio is calculated based on the total liabilities divided by total assets as of the end of the corresponding year/period.

Return on equity

Our Group recorded return on equity ratio of 15.4% and 21.2% respectively for each of the years ended 31 December 2009 and 2010. The increase in the return on equity ratio of our Group in 2010 was mainly due to the significant increase in our net profit as compared to that of 2009. The return on equity ratio of our Group decreased to 3.6% for the six months ended 30 June 2011 due to the lower net profit recognised for the period as compared with that for the full year of 2010. As our tobacco machinery product business is conducted on a project basis, revenue and cost of sales corresponding to our casing and flavouring systems are recognised based on percentage of completion method, whilst revenue and cost of sales corresponding to our other projects and/or products are recognised only upon project completion and/or delivery of products, our return on equity for the six months ended 30 June 2011 is not indicative of our return on equity for the year ending 31 December 2011. For reference, our turnover for the year ended 31 December 2010 was derived from a total of 51 projects undertaken during the year, whereas our turnover for the six months ended 30 June 2011 was derived from a total 24 projects undertaken during the period. For further details on the number of projects undertaken by project category, please refer to the turnover breakdown as set out in the paragraph headed “Our results of operations – Turnover” in this section. During the six months ended 30 June 2011, we have undertaken a number of projects which were not completed as at 30 June 2011. We expect that majority of these contracts will be completed and the corresponding revenue will be recognised by the end of 2011.

Return on assets

For the year ended 31 December 2010, our return on total assets increased slightly to 13.0% from approximately 11.6% for the year ended 31 December 2009 mainly due to the increase in our net profit as compared to that of 2009. The return on asset ratio of our Group decreased to 2.1% for the six months ended 30 June 2011 mainly due to the lower net profit recognised for the period as compared with that for the full year of 2010. Due to the revenue and cost of sales recognition method as discussed above, our return on assets for the six months ended 30 June 2011 is not indicative of our return on assets for the year ending 31 December 2011.

Current ratio

The decrease in the current ratio from 2.7 in 2009 to 2.0 in 2010 was mainly due to the increase in trade and other payables and amount due to a customer for contract work. Our current ratio decreased slightly to 1.9 in the first half of 2011 mainly due to the increase in trade and other payables during the period.

Quick ratio

Our quick ratio remained stable at 1.7 in 2009 and 2010. Our quick ratio decreased to 1.6 in the first half of 2011 mainly due to the increase in trade and other payables during the period.

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Gearing ratio

Our gearing ratio increased from approximately 24.5% in 2009 to 38.6% in 2010 mainly due to the increase in trade and other payables and amount due to a customer for contract work. Our gearing ratio increased to 41.4% in the first half of 2011 mainly due to the increased trade and other payables during the period.

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

Net current assets

	As at 31 December		As at 30 June 2011	As at 31 August 2011
	2009	2010	2011	2011
	HK\$'000	HK\$'000	HK\$'000	HK\$'000 (unaudited)
Current assets				
Inventories	21,851	17,928	22,112	17,618
Trade and other receivables	21,440	42,503	46,511	52,708
Land use rights	68	71	72	72
Amounts due from customers for contract work	3,908	1,614	23,947	38,415
Amount due from ultimate holding company	388	–	–	–
Amounts due from related companies	7,056	417	427	425
Restricted bank deposit	–	237	243	499
Bank balances and cash	5,629	54,383	40,012	30,801
	<u>60,340</u>	<u>117,153</u>	<u>133,324</u>	<u>140,538</u>
Current liabilities				
Trade and other payables	18,029	41,450	68,155	70,948
Amount due to a customer for contract work	–	8,061	–	–
Amounts due to related companies	519	2,500	–	–
Tax payable	3,788	5,959	1,957	2,572
	<u>22,336</u>	<u>57,970</u>	<u>70,112</u>	<u>73,520</u>
Net current assets	<u><u>38,004</u></u>	<u><u>59,183</u></u>	<u><u>63,212</u></u>	<u><u>67,018</u></u>

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The increase in net current assets of approximately HK\$21,179,000 for the year ended 31 December 2010 was mainly due to the increase in trade and other receivables of approximately HK\$21,063,000 and the increase in bank balances and cash of approximately HK\$48,754,000 partially offset by the decrease in inventories of approximately HK\$3,923,000, the decrease in amounts due from related companies of approximately HK\$6,639,000, the increase in trade and other payables of approximately HK\$23,421,000, the increase in amount due to a customer for contract work of approximately HK\$8,061,000 and the increase in tax payable of approximately HK\$2,171,000.

Our net current assets increased by approximately HK\$4,029,000 during the six months ended 30 June 2011 mainly due to the increase in inventories of approximately HK\$4,184,000, increase in trade receivables of HK\$4,008,000, increase in amounts due from customers for contract work of approximately HK\$22,333,000, decrease in amount due to a customer for contract work of approximately HK\$8,061,000, and decrease in tax payable of approximately HK\$4,002,000, which was partially offset by the decrease in bank balances and cash of approximately HK\$14,371,000 and increase in trade and other payables of approximately HK\$26,705,000.

Our unaudited net current assets increased by approximately HK\$3,806,000 for the two months ended 31 August 2011 to approximately HK\$67,018,000 as at 31 August 2011 mainly due to the increase in trade and other receivables of approximately HK\$6,197,000 and the increase in amounts due from customers for contract work of approximately HK\$14,468,000, which was partially offset by the decrease in inventories of approximately HK\$4,494,000, the decrease in bank balances and cash of approximately HK\$9,211,000 and the increase in trade and other payables of approximately HK\$2,793,000. The increase in amounts due from customers for contract work and the decrease in bank balances and cash during the two months ended 31 August 2011 were mainly attributable to the contract costs incurred from a large casing and flavouring system project in progress exceeding the corresponding progress billings charged to our customer up to 31 August 2011. We expect the progress billings in relation to this casing and flavouring system project will be charged to our customer in November 2011. Meanwhile, we have made prepayments to and settled part of the payables with our suppliers in respect of various projects during the two months ended 31 August 2011.

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Cash flow

Overview

During the Track Record Period, our Group's working capital and other capital requirements were principally satisfied by cash generated from its operations.

The following table summarised our Group's cash flows for the period indicated:

	Year ended 31 December		Six months ended 30 June	
	2009	2010	2010	2011
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
			(unaudited)	
Net cash inflow/(outflow)				
from operating activities	9,123	45,454	14,256	(12,005)
Net cash (outflow)/inflow				
from investing activities	(1,321)	1,657	23	(694)
Net cash (outflow)/inflow				
from financing activities	<u>(10,285)</u>	<u>1,429</u>	<u>343</u>	<u>(3,105)</u>
Net cash (decrease)/increase				
in cash and cash equivalents	(2,483)	48,540	14,622	(15,804)
Cash and cash equivalents				
at beginning of the year/period	8,017	5,629	5,629	54,383
Effect of foreign exchange				
rate changes	<u>95</u>	<u>214</u>	<u>46</u>	<u>1,433</u>
Cash and cash equivalents				
at end of the year/period	<u><u>5,629</u></u>	<u><u>54,383</u></u>	<u><u>20,297</u></u>	<u><u>40,012</u></u>

We incurred net operating cash outflow of approximately HK\$12,005,000 and total net cash outflow of approximately HK\$15,804,000 for the six months ended 30 June 2011. Our business is project based and the time needed for completing our projects may vary from 1 month to 9 months depending on the size of our projects. In respect of our tobacco machinery projects, we typically would receive an initial payment ranging from 10% to 30% of the contract value from the customer upon signing the contract and would receive the majority of the payment from our customers upon completion of the project. Therefore, we may have to pay in advance certain costs and expenses in relation to some of the contracts prior to receiving adequate funds to cover such costs and expenses. The net operating cash outflow and total net cash outflow for the six months ended 30 June 2011 were mainly attributable to the increase in inventories and amounts due from customers for contract work and decrease in amount due to a customer for contract work in relation to our projects in progress. The increase in amounts due from customers for contract work during the first half of 2011 was mainly due to the contract costs incurred from the customised casing and flavouring system with movable

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tanks project in progress in Kunming exceeded the corresponding progress billings charged to our customer up to 30 June 2011. We expect the progress billings in relation to this project will be charged to our customer in November 2011. Meanwhile the decrease in amount due to a customer for contract work during the six months ended 30 June 2011 was due to the subsequent contract costs incurred plus recognised profits setting off the progress billing previously charged to this customer in 2010 in relation to the casing and flavouring system with movable tanks project in Kunming. During the period, we also incurred listing expenses of approximately HK\$2,225,000 and paid PRC enterprise income tax of approximately HK\$7,790,000. Notwithstanding that, we did not incur net operating cash outflow for the years ended 31 December 2009 and 31 December 2010.

As our Group did not have any borrowings, mortgages or charges, or material contingent liabilities outstanding as at 31 August 2011, and we had bank balances and cash of approximately HK\$40,012,000 and HK\$30,801,000 as at 30 June 2011 and 31 August 2011 respectively, while the progress billing in respect of the aforementioned casing and flavouring system project is expected to be charged to the customer in November 2011, our Directors are of the view that the net operating cash outflow and overall net cash outflow for the six months ended 30 June 2011 are not likely to have any material adverse impact on our operations.

Operating activities

For the year ended 31 December 2009, our Group recorded a net cash inflow from operating activities of approximately HK\$9,123,000, which was mainly generated from the operating profit before changes in working capital of approximately HK\$18,829,000, adjusted for the outflow of increase in inventories of approximately HK\$5,956,000, the increase in trade and other receivables of approximately HK\$473,000, the increase in amounts due from customers for contract work of approximately HK\$3,908,000, the increase in amounts due from related companies of approximately HK\$236,000, and partially offset by the inflow of increase in trade and other payables of approximately HK\$5,127,000.

For the year ended 31 December 2010, our Group recorded a net cash inflow from operating activities of approximately HK\$45,454,000, which was mainly generated from the operating profit before changes in working capital of approximately HK\$28,267,000, adjusted for the outflow of increase in trade and other receivables of approximately HK\$19,550,000, and partially offset by the inflow of decrease in inventories of approximately HK\$4,523,000, the decrease in amounts due from customers for contract work of approximately HK\$2,426,000, the decrease in amounts due from related companies of HK\$4,504,000, the increase in trade and other payables of approximately HK\$22,773,000 and the increase in amount due to a customer for contract work of approximately HK\$8,061,000.

For the six months ended 30 June 2011, our Group recorded a net cash outflow from operating activities of approximately HK\$12,005,000. While our Group recorded operating cash inflow of approximately HK\$7,274,000 before changes in working capital during the period, the net cash outflow from operating activities was mainly attributable to the increase in inventories of HK\$3,844,000, increase in amounts due from customers for contract work of HK\$22,302,000 and decrease in amount due to a customer for contract work of HK\$8,214,000 in relation to our projects in progress, which was partially offset by the increase in trade and other payables of HK\$25,919,000. During the period,

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our Group also paid PRC enterprise income tax of approximately HK\$7,790,000 which primarily corresponded to the settlement of outstanding tax amount assessed for the year ended 31 December 2010 and the payment of provisional enterprise income tax for the first quarter of 2011.

Investing activities

For the year ended 31 December 2009, the net cash outflow from investing activities amounted to approximately HK\$1,321,000, which was mainly attributable to the advance to related companies of approximately HK\$2,404,000, advance to ultimate holding company of approximately HK\$388,000, purchase of property, plant and equipment of approximately HK\$258,000 and partially offset by the repayment from related companies of approximately HK\$1,644,000 and the receipt of interest of approximately HK\$85,000.

For the year ended 31 December 2010, the net cash inflow from investing activities amounted to approximately HK\$1,657,000, which was mainly attributable to the purchase of property, plant and equipment of approximately HK\$1,103,000, the advance to related companies of approximately HK\$809,000 and increase in restricted bank deposit of approximately HK\$237,000, and partially offset by the repayment from related companies of approximately HK\$3,185,000, the repayment from ultimate holding company of approximately HK\$388,000, the receipt of proceeds from disposal of property, plant and equipment of approximately HK\$23,000 and the receipt of interest of approximately HK\$210,000.

For the six months ended 30 June 2011, the net cash outflow from investing activities amounted to approximately HK\$694,000, which was attributable to the interest received of approximately HK\$157,000, offset by purchase of property, plant and equipment of approximately HK\$851,000.

Financing activities

For the year ended 31 December 2009, our Group recorded a net cash outflow from financing activities amounted to approximately HK\$10,285,000, which primarily consisted of the capital contribution from a shareholder of approximately HK\$999,000, issue of shares of approximately HK\$390,000, advance from related companies of approximately HK\$21,000 and partially offset by the repayment of bank loans of approximately HK\$11,342,000 and interests paid of approximately HK\$353,000.

For the year ended 31 December 2010, our Group recorded a net cash inflow from financing activities amounted to approximately HK\$1,429,000, which primarily consisted of advance from a related company of HK\$2,500,000 and partially offset by repayment to related companies of approximately HK\$539,000.

For the six months ended 30 June 2011, the net cash outflow from financing activities amounted to approximately HK\$3,105,000, which was mainly attributable to further advance from the said related company of HK\$650,000 and the subsequent repayment of amounts due to this related company of HK\$3,150,000 during the period.

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Working capital

Our Directors are of the opinion that after taking into account the amount of the estimated net proceeds of the Placing and our Group's internal resources, we will have sufficient working capital to meet our present requirements for at least the next 12 months from the date of this prospectus.

Inventory and contracts in progress analysis

We generally recognise revenue generated by our projects of casing and flavouring systems on a stage of completion basis. Contracts in progress amounts are presented on the consolidated statement of financial position as amounts due to or from customers for work contracted. Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is shown as amounts due from customers for contract work. For contracts where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is shown as amounts due to customers for contract work. As a result, our inventory balance must be read in light with our contracts in progress information. The inventory balance information, on a stand-alone basis, may not be as meaningful as such information relates to our other products, the turnover of which is recognised when goods are delivered and title has passed.

The following table sets forth the components of our Group's inventories as of 31 December 2009 and 2010 and 30 June 2011:

	At 31 December		As at
	2009	2010	30 June
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Raw materials	7,797	7,379	10,334
Work in progress	14,054	10,549	11,778
Total	<u>21,851</u>	<u>17,928</u>	<u>22,112</u>

Up to 31 August 2011, raw materials of approximately HK\$2,064,000 and work in progress of approximately HK\$4,080,000 which in aggregate represented approximately 27.8% of the inventory balance as at 30 June 2011 were subsequently utilised. The subsequent utilisation of inventory was in line with the expected production schedule and completion schedule of our products. The outstanding work in progress of HK\$7,698,000 principally relates to 19 projects which are expected to be completed between September 2011 and December 2011.

The inventories of our Group comprise raw materials and work in progress. Our Group does not carry any finished goods as all of our products are customised and we will not manufacture our products in advance to meet future demand. The raw materials comprise mainly specialised metallic items, counter modules, steel plates and pipes, electronic devices as well as instruments and meters that are used to produce our tobacco machinery products. The value of our inventories accounted for approximately 36.2%, 15.3% and 16.6% of our total current assets as at 31 December 2009 and 2010 and 30 June 2011 respectively.

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The inventory balance decreased from approximately HK\$21,851,000 as at 31 December 2009 to approximately HK\$17,928,000 as at 31 December 2010. The drop was principally due to the decrease in the balance of work in progress of approximately HK\$3,505,000 from approximately HK\$14,054,000 as at 31 December 2009 to approximately HK\$10,549,000 as at 31 December 2010 as a result of the delivery and completion of 9 projects during the last quarter in 2010, and the related costs of work in progress were recognised as part of the cost of sales in 2010. The inventory balance increased to HK\$22,112,000 as at 30 June 2011 as we had a number of projects in progress, resulting in increase in both raw materials and work in progress balances.

The following table sets forth our average inventory turnover days for the Track Record Period:

	Year ended 31 December		Six months ended
	2009	2010	30 June 2011
Average inventory turnover days (<i>Note</i>)	159	142	83

Note: Average inventory turnover days is calculated based on the average inventory divided by the total cost of sales during the year/period and multiplied by 365 (for the years ended 31 December 2009 and 2010) or 181 (for the six months ended 30 June 2011). Average inventory equals to the sum of inventory balance at the beginning of the year/period and the balance at the end of the year/period and then divided by two.

Our business is project based and our products are highly customised. The time needed for completing our projects may vary from 1 month to 9 months depending on the size of our projects which may differ significantly with the type of products and services provided as well as the complexity of our clients' requirements. Our average inventory turnover days during the Track Record Period were in line with the time generally needed to complete our projects. The decrease in our average inventory turnover days in 2010 was primarily due to the drop in our inventory level resulting from the completion of 9 projects during the last quarter of 2010 and the recognition of the related costs of work in progress as part of the cost of sales for the year ended 31 December 2010. The average inventory turnover days decreased in the first half of 2011 despite the increased inventory level (where the inventory balance did not include those attributable to our contract in progress as explained above) due to the increase in our cost of sales (comprising those for our casing and flavouring systems recognised based on stage of completion basis and those for our other projects recognised upon project completion) resulting from the higher costs associated with the components and devices sourced from independent suppliers for the casing and flavouring system project for a cigarette manufacturer in Kunming during the period.

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The following table sets forth the components of our contracts in progress as of 31 December 2009 and 2010 and 30 June 2011:

	As at 31 December		As at 30 June
	2009	2010	2011
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Contract in progress at the end of the reporting period			
Contract costs incurred plus recognised profits less recognised losses	8,704	24,191	72,737
Less: progress billings	(4,796)	(30,638)	(48,790)
	3,908	(6,447)	23,947
 Analysed for reporting purposes as:			
Amounts due from customers for contract work	3,908	1,614	23,947
Amount due to a customer for contract work	–	(8,061)	–
	3,908	(6,447)	23,947

Amounts due from customers for contract work represented the excess of contract costs incurred plus recognised profits less recognised losses over the progress billings made to our customers as at year end. The amounts due from customers for contract work decreased from approximately HK\$3,908,000 as at 31 December 2009 to approximately HK\$1,614,000 as at 31 December 2010. The decrease was mainly due to the decrease in the contract costs and the increase of progress billings received from our customers as at 31 December 2010, which reduced the amounts due from our customers when compared to the contract costs incurred during the manufacturing of casing and flavouring systems. Amounts due from customers for contract work increased to HK\$23,947,000 as at 30 June 2011 mainly due to the contract costs incurred from a large casing and flavouring system project in progress exceeded the corresponding progress billings charged to our customer up to 30 June 2011 pending the signing of the certificate of normal operation by our customer.

Up to 31 August 2011, the amounts due from customers for contract work in the amount of approximately HK\$398,000, which represented approximately 1.7% of the balance as at 30 June 2011 have been subsequently billed but remained uncollected by our Group. It is expected that such amounts will be settled by the end of 2011. Among the remaining 98.3% of the balance as of 30 June 2011, we expect the progress billings in relation to the aforesaid casing and flavouring system project in progress will be charged to our customer in November 2011, and most of the remaining balance of the amounts due

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from customers for contract work will be billed to our customers by the end of 2011. The progress billings are generally in line with the schedule agreed with the end customers except for amounts due from customers for contract work of approximately HK\$3,204,000 as of 30 June 2011 due to the postponement of delivery schedule as requested by the end customers.

Amount due to a customer for contract work represented the excess of the progress billings made to our customer over the contract costs incurred plus recognised profits less recognised losses as at year end. The amount increased to approximately HK\$8,061,000 as at 31 December 2010 due to the amount of progress billing received in respect to a large casing and flavouring system project exceeding the contract costs incurred up to 31 December 2010. The balance was nil as at 30 June 2011.

Trade and other receivable analysis

The following table sets forth our trade and other receivables as of 31 December 2009 and 2010 and 30 June 2011:

	As at 31 December		As at
	2009	2010	30 June
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Trade receivables	8,870	16,071	16,112
Less: Allowance for doubtful debts	<u>(2,022)</u>	<u>(2,090)</u>	<u>(2,429)</u>
	6,848	13,981	13,683
Prepayments and deposits	3,767	10,192	13,634
Retention money receivables			
– due within one year	6,080	11,272	12,452
Valued added taxes recoverable	–	3,144	2,122
Sundry receivables (net of allowance for doubtful debts)	<u>4,745</u>	<u>3,914</u>	<u>4,620</u>
Total	<u>21,440</u>	<u>42,503</u>	<u>46,511</u>

Trade receivables

During the Track Record Period, our Group normally allowed a credit period of three months to its customers. Before accepting any new customer, our Group will internally assess the credit quality of the potential customer and define appropriate limits.

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The following table sets forth the aging analysis of trade receivables (net of allowance for doubtful debts) as of 31 December 2009 and 2010 and 30 June 2011:

	As at 31 December		As at
	2009	2010	30 June
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>2011</i>
			<i>HK\$'000</i>
0 – 90 days	3,177	9,265	6,525
91 – 365 days	3,326	4,149	6,126
1 – 2 years	147	279	1,032
Over 2 years	198	288	–
	<hr/>	<hr/>	<hr/>
Total	<u>6,848</u>	<u>13,981</u>	<u>13,683</u>

During the Track Record Period, we generally granted a credit term of 90 days to CTMC and our other customers. As at 31 December 2009 and 2010 and 30 June 2011, our trade receivables were due from customers other than CTMC.

Our Group's trade receivables (net of allowance for doubtful debts) amounted to HK\$6,848,000 as at 31 December 2009. Our Group's trade receivables included receivables with carrying amount of HK\$3,671,000 which were past due but not impaired as at 31 December 2009 as there has not been a significant change in credit quality and the amounts were considered recoverable. Our Group's trade receivables (net of allowance for doubtful debts) amounted to HK\$13,981,000 as at 31 December 2010. Our Group's trade receivables included receivables with carrying amount of HK\$4,716,000 which were past due but not impaired as at 31 December 2010 as there had not been a significant change in credit quality and the amounts were considered recoverable. Of these past due but not impaired amounts, approximately HK\$3,185,000 was due from three cigarette manufacturers as additional modifications were requested by these customers. Settlement amount of approximately HK\$1,517,000 has been subsequently received as of 31 August 2011, whilst the remaining balance will be settled by the customers pending their internal payment process.

Our Group's trade receivables (net of allowance for doubtful debts) amounted to HK\$13,683,000 as at 30 June 2011. Our trade receivables included receivables with carrying amount of HK\$7,158,000 which were past due but not impaired as at 30 June 2011 as there had not been a significant change in credit quality and the amounts were considered recoverable. Up to 31 August 2011, approximately HK\$2,286,000 of the overdue amount was subsequently settled. Of the outstanding balance of approximately HK\$4,872,000, an aggregate amount of HK\$4,301,000 was due from eight customers, each with overdue amount exceeding HK\$200,000. The slow settlement was mainly due to additional modifications requested by our customers and delay in the customers' internal payment process to settle their balances due to us. It is currently expected that the relevant modifications would be completed in the fourth quarter of 2011. Provisions for doubtful debt of approximately HK\$288,000 were made during the six months ended 30 June 2011 after considering the nature of the trade receivables and their collectability.

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Up to 31 August 2011, the trade receivables in the amount of approximately HK\$5,925,000, which represented approximately 43.3% of the net balance as at 30 June 2011 have been subsequently settled. We also recovered approximately HK\$120,000 of long outstanding balance, which was provided for as doubtful debt as at 30 June 2011, during the two months ended 31 August 2011.

We monitor the recoverability of our trade receivables on a monthly basis. With respect to the overdue trade receivables, we will designate our sales and marketing employees to collect these receivables. Moreover, the general manager, the vice general manager as well as the head of sales and marketing department of Baoying Renheng pay regular visits to our customers to update the project status and to follow up directly with customers in respect of overdue payment.

The net trade receivable balance has increased by approximately HK\$7,133,000 during the year ended 31 December 2010 which was in line with the growth of the business of the Group, and considerable projects were completed and delivered during the last quarter of the year with such trade balances not due for settlement by customers. Meanwhile, the trade receivables balance decreased slightly by HK\$298,000 to HK\$13,683,000 as at 30 June 2011 which was mainly attributable to the increase of our trade balances with customers attributable to projects undertaken during the period, offset by the collection of our trade receivables brought forward from previous year. As at 31 December 2009 and 2010 and 30 June 2011, our Group did not hold any collateral over the trade receivable balance.

The following table sets forth our average trade receivables turnover days for the Track Record Period:

	Six months ended		
	Year ended 31 December		30 June
	2009	2010	2011
Average trade receivables turnover days (<i>Note</i>)	44	41	39

Note: Average trade receivables turnover days are computed by the average net trade receivable balance divided by the turnover for the year/period and multiplied by 365 (for the years ended 31 December 2009 and 2010) or 181 (for the six months ended 30 June 2011). Average net trade receivable equals to the sum of net trade receivable balance at the beginning of the year/period and the net trade receivable balance at the end of the year/period and then divided by two.

During the Track Record Period, the average trade receivables turnover days were quite stable and remained within the credit period of three months normally granted to our customers.

FINANCIAL INFORMATION

Prepayments and deposits

Prepayments and deposits mainly comprise prepaid expenses and deposits paid to suppliers. The balance has increased by approximately HK\$6,425,000 from approximately HK\$3,767,000 as at 31 December 2009 to approximately HK\$10,192,000 as at 31 December 2010 which was mainly attributable to the prepayments of listing expenses of approximately HK\$812,000 and prepayments of approximately HK\$5,613,000 paid to our suppliers. We have secured more contracts for catalogued special-purpose tobacco machinery products during 2010 and thus more prepayments to our suppliers were made in order to secure the supply of our raw materials in early 2011. The prepayments and deposits increased by approximately HK\$3,442,000 to HK\$13,634,000 as at 30 June 2011 which was mainly attributable to the increase in prepayments of listing expenses to approximately HK\$1,673,000 and the increase in prepayments to our suppliers to approximately HK\$11,420,000 for securing the supply of our raw materials, parts and components for ongoing projects in 2011.

Retention money receivables – due within one year

Retention money receivables refer to the sum retained by our customers after the delivery and completion of the contracts but before the expiry of the warranty period given by our Group, which in general, a period of 12 months. The retention money usually presents a specific percentage of the contract value. The balance has increased by approximately HK\$5,192,000 from approximately HK\$6,080,000 as at 31 December 2009 to approximately HK\$11,272,000 as at 31 December 2010 which was in line with the growth of our business, with more contracts completed and revenue generated. The balance increased by HK\$1,180,000 to HK\$12,452,000 as at 30 June 2011 mainly attributable to the increase in retention money receivables in relation to projects completed, which was partially offset by the retention money receivables settled by our customers.

The retention money receivables will become due for payment by our customers upon the expiry of warranty period given by our Group. The following table sets forth a breakdown of retention money receivables as of 31 December 2009 and 2010 and 30 June 2011:

	As at 31 December		As at
	2009	2010	30 June
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Amounts not due for payment	5,879	7,375	9,079
Overdue amounts	201	3,897	3,373
Total	6,080	11,272	12,452

It is expected that the amounts not due for payment as of 30 June 2011 will be received by our Group by mid 2012.

FINANCIAL INFORMATION

As of 30 June 2011, the overdue amount included an amount to be released by CTMC of approximately HK\$2,386,000 pending receipt of the signed original acknowledgements of inspection from our end customers for submission to CTMC as the end customers require additional time to process the original acknowledgements of inspection. To expedite the release of the retention money, the general manager of Baoying Renheng as well as the sales manager and the technical personnel in-charge of the relevant projects have closely liaised with our end customers in respect of the outstanding original acknowledgements of inspection and will continue to monitor the progress. We expect that such amount will be released by the end of 2011. Up to 31 August 2011, none of the overdue amount as at 30 June 2011 was subsequently settled.

Sundry receivables

Sundry receivables mainly comprise advances to staff and deposits for tender. The following table sets forth a breakdown of our sundry receivables as of 31 December 2009 and 2010 and the six months ended 30 June 2011:

	As at 31 December		As at
	2009	2010	30 June
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Advances to staff	3,149	2,435	3,568
Deposits for tender	1,596	1,479	1,005
Utilities deposits	—	—	47
	<hr/>	<hr/>	<hr/>
Total	<u>4,745</u>	<u>3,914</u>	<u>4,620</u>

The advances to staff were mainly used to cover entertainment, travelling and transportation expenses as well as payments for purchasing spare parts for installation use at the end customers' sites.

FINANCIAL INFORMATION

Trade and other payables analysis

The following table sets forth our trade and other payables as of 31 December 2009 and 2010 and the six months ended 30 June 2011:

	As at 31 December		As at
	2009	2010	30 June
	<i>HK\$'000</i>	<i>HK\$'000</i>	2011
Trade payables	11,634	21,999	49,046
Advances from customers	3,074	16,595	16,326
Accrued welfare expense	1,634	1,690	1,728
Valued added tax payable	536	–	–
Other payables	1,151	1,166	1,055
	<u>11,634</u>	<u>21,999</u>	<u>49,046</u>
Total	<u>18,029</u>	<u>41,450</u>	<u>68,155</u>

The following table sets forth the aged analysis of trade payables based on the invoice date as of 31 December 2009 and 2010:

	As at 31 December		As at
	2009	2010	30 June
	<i>HK\$'000</i>	<i>HK\$'000</i>	2011
0 – 90 days	9,734	18,831	44,411
91 – 365 days	1,629	1,833	3,442
1 – 2 years	11	1,064	913
Over 2 years	260	271	280
	<u>11,634</u>	<u>21,999</u>	<u>49,046</u>
Total	<u>11,634</u>	<u>21,999</u>	<u>49,046</u>

The trade payables as at 30 June 2011 of approximately HK\$20,811,000, which represented approximately 42.4% of the total balance, have been subsequently settled up to 31 August 2011.

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The following table sets forth our average trade payables turnover days for the Track Record Period:

	Year ended 31 December 2009	2010	Six months ended 30 June 2011
Average trade payables turnover days (<i>Note</i>)	60	115	84

Note: Average trade payables turnover days are computed by the average trade payable balances for the year/period, divided by the total amount of purchase of goods for the year/period and multiplied by 365 (for the year ended 31 December 2009 and 2010) or 181 days (for the six months ended 30 June 2011). Average trade payable equals to the trade payable balance at the beginning of the year/period plus trade payable balance at the end of the year/period and divided by two.

The credit periods granted by our suppliers range from 30 to 90 days. Average trade payable turnover days were approximately 60 days, 115 days and 84 days in 2009, 2010 and the first six months of 2011 respectively. The increase in the trade payables turnover days in 2010 was mainly attributable to our purchases in December 2010 of approximately HK\$6,400,000, representing approximately 12.0% of our aggregate purchases of raw materials, parts and components during 2010. As at 31 December 2010, over 85% of the outstanding trade payables were aged within 90 days and the trade payables relating to our purchases in December 2010 were not due for payment at the end of the year. The trade payables turnover days decreased to 84 days during the first six months of 2011 despite the increase in our trade payables balance as at 30 June 2011 mainly due to more purchases made to fulfill our projects' needs in the first half of 2011 and expected projects' needs for the second half of 2011, which amounted to approximately HK\$76,817,000 for the six months ended 30 June 2011, as compared to our full year purchase of approximately HK\$53,149,000 for the year ended 31 December 2010. We have settled most of the outstanding balance according to the credit terms granted by the suppliers during the Track Record Period and up to the Latest Practicable Date. Our Directors confirmed that our Group had not encountered any financial difficulties in fulfilling its payment obligations and its relationship with suppliers had not been adversely affected during the Track Record Period and up to the Latest Practicable Date.

Advances from customers

Our Group receives advance payment from customers for projects after the relevant contracts are signed. In general, the percentage varies from 10% to 30%, depending on the nature of the contracts. The balance has increased by approximately HK\$13,521,000 from approximately HK\$3,074,000 as at 31 December 2009 to approximately HK\$16,595,000 as at 31 December 2010 which was mainly due to the receipts of advance payments of approximately HK\$12,977,000 from our customers in respect of casing and flavouring systems and PF systems contracted. The balance decreased by approximately HK\$269,000 to approximately HK\$16,326,000 as at 30 June 2011 which was mainly attributable to the commencement of our casing and flavouring system project and the completion of other projects during the period, partly offset by the advance payments received in relation to contracted projects which have not been completed during the period.

FINANCIAL INFORMATION

Other payables

Set out below is the breakdown of our Group's other payables as at 31 December 2009 and 2010 and 30 June 2011:

	As at 31 December		As at
	2009	2010	30 June
	HK\$'000	HK\$'000	2011
Audit fee	600	350	263
Labor union fee	44	119	89
Others	507	697	703
	<hr/>	<hr/>	<hr/>
Total	<u>1,151</u>	<u>1,166</u>	<u>1,055</u>

Capital commitments

As at 31 December 2009, 31 December 2010 and 30 June 2011, our Group did not have any significant capital commitments respectively.

QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

We are exposed to various types of market risks, including liquidity risk, foreign exchange risk, commodity price risk, interest rate risk and inflation risk.

Liquidity risk

The Board and the finance manager of our Group regularly monitor our Group's present and future cashflow requirements in order to ensure that our Group maintains sufficient funding readily available for its day-to-day operations, planned capital expenditure and scheduled bank loan repayment.

For each of the two years ended 31 December 2009 and 2010 and the six months ended 30 June 2011, our Group financed its operations and current liabilities through internally generated cash flow. As at 31 December 2009 and 2010 and 30 June 2011, our Group's bank balances and cash amounted to approximately HK\$5,629,000, HK\$54,383,000 and HK\$40,012,000 respectively and we did not have any banking facilities as at 30 June 2011. We applied for bank loans as and when required, and our bank loans were fully repaid in 2009. Our Directors confirmed that no banking facilities of our Group had been cancelled by its banks during the Track Record Period. Our Directors consider that our Group is not exposed to any significant liquidity risk.

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Foreign exchange risk

Our financial statements are expressed in Hong Kong dollars, whilst currency for its operations in the PRC is RMB. Therefore, any depreciation of RMB will reduce the value of our Group's assets and profitability and any dividends payable on the Shares in Hong Kong dollars terms. Our manufacturing operation is based in the PRC and all of the sales and costs of sales are denominated in RMB. Any appreciation of RMB against Hong Kong dollars will increase the amount of turnover and profit which was originally accounted for in RMB and converted to Hong Kong dollars as reported in the accounts of our Company.

As at the Latest Practicable Date, our Group has not entered into any hedging transactions to reduce its foreign currency exposure, as the availability of hedge instrument is limited in the PRC.

In addition, we will need to remit the proceeds from the Placing into the PRC and convert them into RMB. The PRC Government may restrict such remittance and conversion. The value of RMB against other currencies may fluctuate and is affected by, among other things, changes in the PRC political and economic conditions. The conversion of RMB into foreign currencies, including Hong Kong dollars, has been based on rates set by the PBOC.

Commodity price risk

While we price our catalogued products in accordance with (i) the 5% range of the guidance price in the Pricing Guidelines; and (ii) the Pricing Approval 2010, we determine the contract price based on our estimated project costs plus a mark-up margin at the time we submit a proposal to our potential customers or our tenders for projects. After we have entered into a sales contract with our customers, we may then procure the necessary raw materials, parts and components. There is a time lapse between the submission of proposals or tenders and the procurement of raw materials, parts and components. Any changes in the prices of raw materials, parts and components during this interim period will affect our profitability.

Interest rate risk

Our exposure to the risk of changes in market interest rates primarily relates to our interest-bearing borrowings. As of 30 June 2011, we had no bank borrowings. We do not anticipate a significant impact resulting from changes in interest rates as interest bearing bank balances are within short maturity period. We have not historically used, and do not expect to use in the future, any derivative financial instruments to manage our interest rate exposure.

FINANCIAL INFORMATION

INDEBTEDNESS

Borrowings and banking facilities

As at 31 August 2011, our Group had no banking facilities and had no borrowings outstanding.

Security

As at 31 August 2011, our Group did not have any mortgages or charges.

Contingent liabilities

As at 31 August 2011, our Group did not have any material contingent liabilities.

Disclaimer

Up to the Latest Practicable Date, our Group had no outstanding mortgages, charges, debentures or other loan capital or bank overdrafts, loans or other similar indebtedness or hire purchase commitments or finance lease commitments or any guarantees or other material contingent liabilities.

Our Directors have confirmed that there have been no material changes in the indebtedness and contingent liabilities of our Group since 31 August 2011.

PROPERTY INTERESTS AND PROPERTY VALUATION

Greater China Appraisal Limited, an independent property valuer, has valued the property interests of our Group as at 31 August 2011 at RMB39,100,000 or approximately HK\$46,894,000. The full text of the letter with a summary of valuation and valuation certificates in connection with our Group's property interests are set out in Appendix III to this prospectus.

FINANCIAL INFORMATION

The table below sets forth the reconciliation of aggregate amounts of property interests from our Group's audited consolidated financial statements as at 30 June 2011 to their value as at 31 August 2011 as stated in Appendix III to this prospectus:

	<i>HK\$'000</i>
Net book value of property interests as at 30 June 2011 as per Appendix I to this prospectus:	
Buildings	12,113
Land use rights	3,107
Investment properties	<u>18,999</u>
	34,219
Movements for the two months ended 31 August 2011:	
Depreciation on buildings (unaudited)	(126)
Amortisation on land use rights (unaudited)	<u>(12)</u>
Net book value of properties interests as at 31 August 2011	34,081
Revaluation surplus	<u>12,813</u>
Valuation of property interests as at 31 August 2011 as set out in Appendix III to this prospectus	<u><u>46,894</u></u>

OFF BALANCE SHEET TRANSACTIONS

We have not entered into any material off balance sheet transactions or arrangements during the Track Record Period.

DIVIDEND POLICY

During the Track Record Period, and up to the Latest Practicable Date, save for intra-group dividend declared to Renheng Tech from Baoying Renheng, we did not declare any dividends. As at the Latest Practicable Date, our Directors had no intention to distribute any other profits from Baoying Renheng. Our Company does not have any pre-determined dividend distribution ratio. The payment and the amount of any dividends, if paid, will depend on the results of operations, cash flows, financial condition, statutory and regulatory restrictions on the payment of dividends by our Group, future prospects and other factors that our Directors may consider relevant. The declaration, payment and amount of dividends will be subject to our Group's discretion. Dividends may be paid only out of the distributable profits as permitted under the relevant laws. To the extent profits are distributed as dividends, such portion of profits will not be available to be reinvested in our Group's operations. There can be no assurance that our Group will be able to declare or distribute any dividend in the amount set out in any plan of our Board or at all. The dividend distribution record in the past may not be used as a reference or basis to determine the level of dividends that may be declared or paid by our Group in the future.

FINANCIAL INFORMATION

UNAUDITED PRO FORMA ADJUSTED NET TANGIBLE ASSETS

The statement of unaudited pro forma adjusted net tangible assets of our Group is set out below to illustrate the effect of the Placing on the audited consolidated net tangible assets of our Group as if the Placing had taken place on 30 June 2011. The statement of unaudited pro forma adjusted net tangible assets of our Group has been prepared for illustrative purposes only and, because of its nature, may not give a true picture of the financial position of our Group following the Placing.

The following statement of unaudited pro forma adjusted net tangible assets of our Group is based on the audited consolidated net tangible assets of our Group attributable to the owners of our Company as at 30 June 2011 as shown in the accountants' report of the financial information of our Group, the text of which is set out in Appendix I to this prospectus, and adjusted as follows:

	Audited consolidated net tangible assets of our Group attributable to the owners of our Company as at 30 June 2011 HK\$'000 (Note a)	Estimated net proceeds from the Placing HK\$'000 (Note b)	Unaudited pro forma adjusted net tangible assets of our Group attributable to the owners of our Company HK\$'000	Unaudited pro forma adjusted net tangible assets per Share HK\$ (Note c)
Based on the Placing Price of HK\$1.10 per Share	<u>99,934</u>	<u>46,291</u>	<u>146,225</u>	<u>0.73</u>
Based on the Placing Price of HK\$1.30 per Share	<u>99,934</u>	<u>55,940</u>	<u>155,874</u>	<u>0.78</u>

Notes:

- (a) The audited consolidated net tangible assets of our Group attributable to the owners of our Company as at 30 June 2011 has been derived from the net assets of our Group attributable to the owners of our Company as shown in the accountants' report of the financial information of our Group set out in Appendix I to this prospectus.
- (b) The estimated net proceeds from the Placing are based on 50,000,000 Shares at the Placing Price of HK\$1.10 and HK\$1.30 per Share, after deduction of estimated related fees and expenses (excluding listing expenses of approximately HK\$3,820,000 charged to profit or loss during the two years ended 31 December 2010 and the six months ended 30 June 2011).
- (c) The number of shares used for the calculation of unaudited pro forma adjusted net tangible assets per Share is based on 200,000,000 Shares in issue immediately after the Placing but takes no account of any Shares which may be issued upon the exercise of options that may be granted under the Pre-IPO Share Option Scheme and the Share Option Scheme.

FINANCIAL INFORMATION

- (d) As of 31 August 2011, our Group's property interests were valued by Greater China Appraisal Limited, an independent property valuer, and the relevant property valuation report is set out in Appendix III to this prospectus. The revaluation surplus, representing the excess of market value of the properties over their book value, is approximately HK\$12,813,000. Such revaluation surplus has not been incorporated in our Group's consolidated financial information for the six months ended 30 June 2011 and will not be incorporated in our Group's consolidated financial statements for the year ending 31 December 2011. The above adjustment does not take into account the above revaluation surplus. Had the properties been stated at such valuation, an additional depreciation of approximately HK\$574,000 per annum would have been charged against profit or loss.

DISTRIBUTABLE RESERVES

There was no reserve available for distribution to the Shareholders as at 30 June 2011, as our Company was incorporated on 2 February 2011. It has not carried out any business since the date of its incorporation save for the transactions related to the Reorganisation.

DISCLOSURE UNDER CHAPTER 17 OF THE GEM LISTING RULES

Our Directors have confirmed that, as at the Latest Practicable Date, they were not aware of any circumstances which would give rise to a disclosure requirement under Rules 17.15 to 17.21 of the GEM Listing Rules.

NO MATERIAL ADVERSE CHANGE

Our Directors confirm that there has been no material adverse change in the financial trading position of our Group since 30 June 2011, being the date to which the latest audited financial statements of our Group were made up.

DIRECTORS, SENIOR MANAGEMENT AND STAFF

BOARD OF DIRECTORS

Our Board is responsible and has general powers for the management and conduct of our business. The table below sets forth certain information concerning our Directors:

Name	Age	Position	Date of appointment	Key role
Mr. Wei	44	Chairman and executive Director	2 February 2011	Overall business planning and strategic development of our Group
Ms. Liu	41	Executive Director	2 February 2011	Overseeing the human resources and administration functions of our Group
Mr. Sun Zhaohui (孫朝暉)	44	Executive Director and chief executive officer	20 October 2011	Overall management and corporate development of our Group as well as acquisition and strategy implementation of Baoying Renheng
Mr. Tam Yuk Sang Sammy (譚旭生)	48	Independent non-executive Director	20 October 2011	Overseeing our Group's management and strategic development
Mr. Wong Yiu Kit (黃耀傑)	44	Independent non-executive Director	20 October 2011	Overseeing our Group's management and strategic development
Mr. Kong Hing Ki (江興琪)	40	Independent non-executive Director	20 October 2011	Overseeing our Group's management and strategic development

Executive Directors

Mr. Wei, aged 44, is an executive Director, the chairman of our Board, and one of the founders of Baoying Renheng. Mr. Wei was appointed as a Director with effect from 2 February 2011 and was redesignated as an executive Director with effect from 20 October 2011. Mr. Wei is also the director of two subsidiaries of our Company, namely Renheng Global and Renheng Tech, appointed on 15 October 2009 and 28 October 2009 respectively. Mr. Wei is primarily responsible for the overall business planning and strategic development of our Group. Mr. Wei served as the personal assistant of Mr. Zhong Sheng Jian between 1987 and 1996 in managing Mr. Zhong's private investments principally in the PRC. Mr. Wei emigrated from the PRC to the Republic of Singapore and became a citizen there in or around December 1994. Since October 1999, Mr. Wei has been living in Hong Kong. Mr. Wei

DIRECTORS, SENIOR MANAGEMENT AND STAFF

has more than 14 years of experience in the electrical and mechanical equipment industry. Between October 1996 to July 2001, Mr. Wei was the legal representative of Zhuhai Special Economic Zone Ren Heng Electromechanical Company Limited (珠海經濟特區仁恒機電有限公司), a company incorporated in the PRC with a business scope of manufacturing and selling automatic machinery, electrical and electronic products as well as tobacco related machinery products. As a founding member of Baoying Renheng, Mr. Wei has gained knowledge and experience in the tobacco machinery industry during the last 10 years. Mr. Wei was a director and the legal representative of Baoying Renheng between November 2001 and March 2005, and he has served as the director of the holding companies of Baoying Renheng including Yanlord Industrial since August 1992 and Yanlord Industry Investment since May 2005 to monitor the operation of Baoying Renheng. Mr. Wei graduated from Lufeng County Donghai Secondary School* (陸豐縣東海中學) in July 1987. In the last three years, he did not hold any directorship in any publicly listed company. Mr. Wei is the spouse of Ms. Liu.

Mr. Wei has entered into a service contract with our Company for a term of three years commencing on 20 October 2011.

Ms. Liu, aged 41, is an executive Director. Ms. Liu was appointed as a Director with effect from 2 February 2011 and was redesignated as an executive Director with effect from 20 October 2011. She is responsible for overseeing the human resources and administration functions of our Group. Ms. Liu was appointed as a director of Grand Bright, the holding company of Zhuhai Mingtai, since November 1999. Ms. Liu was also appointed as a director of GrandBright International Pte. Ltd., a company engaged in the manufacture of furniture and fixture primarily made of metal, since February 2006. She is principally responsible for the treasury, human resources and administrative functions of the company. In February 2007, Ms Liu was appointed as a director of Yanlord Industry Investment and has been responsible for overseeing the operation of Baoying Renheng thereafter since the completion of the transfer of 91.6% equity interest in Baoying Renheng from Yanlord Industrial to Yanlord Industry Investment in 2008. Ms. Liu obtained a bachelor's degree in sport management from Beijing Sport University (北京體育大學) (formerly known as Beijing Institute of Physical Education (北京體育學院)) in July 1992. Ms. Liu immigrated to Hong Kong in 1999 and has been living in Hong Kong since then. In the last three years, she did not hold any directorship in any publicly listed company. Ms. Liu is the spouse of Mr. Wei.

Ms. Liu has entered into a service contract with our Company for a term of three years commencing on 20 October 2011.

Mr. Sun Zhaohui (孫朝暉), aged 44, is an executive Director, the chief executive officer of our Company and the legal representative of Baoying Renheng. Mr. Sun was appointed as an executive Director with effect from 20 October 2011. In May 2008, Mr. Sun accepted the invitation from Mr. Wei to be the legal representative of Baoying Renheng, whilst he was working as the general manager of Quantum Automation (Shanghai) Co., Ltd. ("Shanghai Quantum") (上海貫通自控系統有限公司). Mr. Sun has confirmed that he obtained verbal consent from Shanghai Quantum when accepting the appointment of the legal representative of Baoying Renheng and spent approximately 50% of his time in Baoying Renheng. In March 2010, Mr. Sun left Shanghai Quantum and started to devote 100% of his time in our Group.

DIRECTORS, SENIOR MANAGEMENT AND STAFF

Mr. Sun is primarily responsible for the overall management and corporate development, acquisition and strategy implementation of Baoying Renheng. He has accumulated no less than 10 years of experience in engineering field. Mr. Sun joined IPACS Asia Pte Ltd. as a senior engineer in October 1997, and subsequently took up the position of vice general manager of IPACS Computer System Engineering (Shanghai) Co. Ltd. (宇博計算機系統工程(上海)有限公司) in December 1999. Mr. Sun then worked as the general manager of Shanghai Quantum for over 8 years from September 2001 to March 2010. Mr. Sun graduated with a bachelor's degree in engineering mechanics from Harbin Institute of Technology (哈爾濱工業大學) in July 1990. In the last three years, he did not hold any directorship in any publicly listed company.

Mr. Sun has entered into a service contract with our Company for a term of three years commencing on 20 October 2011.

Independent non-executive Directors

Mr. Tam Yuk Sang, Sammy (譚旭生), aged 48, is our independent non-executive Director and the chairman of the nomination committee, and a member of the remuneration committee and the audit committee of the Company. Mr. Tam was appointed as an independent non-executive Director with effect from 20 October 2011. He has over 20 years of experience in accounting, auditing and finance. He is currently president of Essentack Limited, a corporate strategy and management advisory company. He is an independent non-executive director and the audit committee chairman of Kith Holdings Limited (stock code: 1201), a company whose shares are listed on the Stock Exchange, and also an independent non-executive director of KEE Holdings Company Limited (stock code: 2011), a company whose shares are listed on the Stock Exchange. Mr. Tam served as the chief financial officer of Ngai Lik Industrial Holdings Limited (stock code: 332), a company whose shares are listed on the Stock Exchange, from August 1993 to January 2000 and general manager of Tom.Com International Limited from February 2000 to July 2001. Mr. Tam was the chief financial officer of Chen Hsong Holdings Limited (stock code: 57), a company whose shares are listed on the Stock Exchange, from 2001 to 2002. In the three years preceding the Latest Practicable Date, Mr. Tam was also an independent non-executive director of Ngai Lik Industrial Holdings Limited (stock code: 332), a company whose shares are listed on the Stock Exchange, from 2004 to 2010, and he also served as the audit committee chairman of Ngai Lik Industrial Holdings Limited between 2006 and 2009. Mr. Tam obtained from the Hong Kong Polytechnic University a professional diploma in accountancy in November 1986 and is a fellow of The Association of Chartered Certified Accountants and the Hong Kong Institute of Certified Public Accountants.

Mr. Wong Yiu Kit (黃耀傑), aged 44, is an independent non-executive Director and the chairman of the audit committee, and a member of the remuneration committee and the nomination committee of the Company. Mr. Wong was appointed as an independent non-executive Director with effect from 20 October 2011. Mr. Wong has over 14 years of experience in venture capital, corporate finance, business development, financial and general management. He joined China Private Equity Investment Holdings Limited in April 2008, a company focusing on private equity investment and listed on the Alternative Investment Market of the London Stock Exchange Plc in 2008, and is now the executive director and chief financial officer of the company. Before that, he was the manager and head of supervision of business department of Guangdong Investment Limited (stock code: 270), a company whose shares are listed on the

DIRECTORS, SENIOR MANAGEMENT AND STAFF

Stock Exchange, from August 1997 to June 2000, the vice president of Vertex Management (HK) from July 2000 to October 2002, the chief financial officer of Hong Kong Applied Science and Technology Research Institute Company Limited from November 2002 to April 2008. Mr. Wong obtained a bachelor's degree in business administration from the University of Hong Kong in November 1991, a master of science in investment management from the Hong Kong University of Science and Technology in November 1998, and a master of science in Electronic Engineering from the Chinese University of Hong Kong in December 2008. Mr. Wong is a fellow member of the Hong Kong Institute of Certified Public Accountants and the Association of Chartered Certified Accountants, and an associate member of the Institute of Chartered Accountants in England and Wales. He is also a charter-holder of Chartered Financial Analyst and a member of Hong Kong Securities Institute.

Mr. Kong Hing Ki (江興琪), aged 40, is our independent non-executive Director and the chairman of the remuneration committee, and a member of the audit committee and the nomination committee of the Company. Mr. Kong Hing Ki was appointed as an independent non-executive Director with effect from 20 October 2011. He has over 10 years of experience in accounting, auditing and finance, gained from accountancy and commercial firms. Currently, he is a financial controller of a company whose ultimate holding company is listed on the main board of the Singapore Exchange Securities Trading Limited, and is an independent non-executive director and the audit committee chairman of Hing Lee (HK) Holdings Limited (stock code: 396), a company whose shares are listed on the Stock Exchange, and also an independent non-executive director of KEE Holdings Company Limited (stock code: 2011), a company whose shares are listed on the Stock Exchange. Mr. Kong obtained a Bachelor's Degree in Commerce from The Australian National University and a Master of Business Administration Degree from Deakin University, which is a joint program of Deakin University and CPA Australia conducted in Hong Kong. He is a Fellow of the Hong Kong Institute of Certified Public Accountants and a member of CPA Australia.

Each of our independent non-executive Directors, by themselves or through the companies in which they work for, do not and have never provided any service to our Company during the Track Record Period.

Save as disclosed in this prospectus, there are no other matters concerning all our Directors' appointment that need to be brought to the attention of our Shareholders and the Stock Exchange and there are no other matters which should be disclosed pursuant to Rule 17.50(2) of the GEM Listing Rules.

SENIOR MANAGEMENT

Mr. Xu Jiagui (徐加貴), aged 44, is the director and general manager of Baoying Renheng. Mr. Xu is primarily responsible for the strategic planning, business development as well as overseeing the daily operations of Baoying Renheng. Mr. Xu has over 8 years of experience in research and development, production and general management relating to the tobacco machinery manufacturing industry. Mr. Xu was the vice general manager of Baoying Radio Factory (寶應縣無線電廠) until December 2001. He subsequently joined Baoying Renheng in January 2002 as a result of the ownership reform program of Baoying Radio Factory as discussed in the paragraph headed "Corporate development" in the section headed "History and development" of this prospectus. Mr. Xu was awarded by Baoying County top

DIRECTORS, SENIOR MANAGEMENT AND STAFF

ten technological worker (十佳科技工作者) and advanced technological worker (先進科技工作者) in March 2000 and April 2001 respectively. He graduated with a college diploma in mechanical design and manufacturing process from Jiangsu Radio and TV University (江蘇廣播電視大學) in July 1991 and obtained a certificate of completion for Class for Advanced Studies of Postgraduate Curricula (研究生課程進修班結業證書) in management science and engineering (管理科學與工程專業進修碩士研究生課程) from Southeast University (東南大學) in December 2004. In the last three years, he did not hold directorship in any publicly listed company.

Mr. Liu Yang (劉洋), aged 38, is a director and vice general manager of Baoying Renheng. He is principally responsible for overseeing the sales and marketing activities of Baoying Renheng. Mr. Liu has over 14 years of experience in sales and marketing. He was the vice general manager for sales of Zhuhai Gang Zhuhai Ming An Enterprise Co. Ltd. (珠海市珠海港明安企業有限公司) between July 1994 to June 2002, and subsequently acquired knowledge and experience in the tobacco machinery industry after joining Baoying Renheng in June 2004. He graduated with a bachelor's degree in marketing from Changchun University of Science and Technology (長春理工大學) (formerly known as Changchun Institute of Optics and Fine Mechanics (長春光學精密機械學院)) in July 1993. In the last three years, Mr. Liu did not hold any directorship in any publicly listed company. Mr. Liu is the brother of Ms. Liu.

Mr. An Zhanqi (安戰旗), aged 53, is the chief engineer of Baoying Renheng and is the head of the technical department, the production department as well as the procurement department of our Group. Mr. An has no less than 9 years of experience in the engineering field. He was the general manager of Yanlord Industrial (Shenzhen) Co., Ltd.* (仁恒實業(深圳)有限公司) from April 1995 to June 1996 and was appointed as the general manager of Zhuhai Special Economic Zone Ren Heng Electromechanical Company Limited* (珠海經濟特區仁恒機電有限公司) from July 1996 to December 1997. Mr. An was the chief engineer of a company engaged in the provision of environmental technology consultancy services between 2001 and 2005 prior to joining our Group in January 2006. He graduated with a bachelor's degree in chemical engineering from Tsinghua University (清華大學) in November 1982. In the last three years, he did not hold any directorship in any publicly listed company.

Mr. Ho Pui Lam Joseph (何沛霖), aged 31, is the company secretary of our Company and a finance manager of our Group. Mr. Ho is a member of the Hong Kong Institute of Certified Public Accountants and has over 7 years of experience in the audit and accounting profession. Prior to joining our Group on 1 December 2010, Mr. Ho worked as an audit manager in an international accounting firm. He obtained a bachelor's degree in accounting and finance from the University of Hong Kong in December 2002. In the last three years, he held no directorship in any publicly listed company.

COMPLIANCE OFFICER

Mr. Sun Zhaohui is the compliance officer of our Company. His biography is set out in the paragraph headed "Executive Directors" in this section of the prospectus.

DIRECTORS, SENIOR MANAGEMENT AND STAFF

REMUNERATION POLICY

Our Directors and senior management are remunerated in the form of salaries and bonus determined by reference to their respective experience, responsibilities, qualifications and competence displayed and the operating results of our Group. They also receive reimbursements for expenses which are necessarily and reasonably incurred for providing services to our Group or executing their functions in relation to our operations. Our Directors and senior management may also receive options granted under the Share Option Scheme after the Listing.

STAFF

As at 31 August 2011, our Group had a total of 147 employees. The following table sets forth the breakdown of our employees by function and location.

	Hong Kong	PRC	Total
Management	2	2	4
Sales and marketing	–	12	12
Production	–	52	52
Procurement	–	4	4
Technical	–	37	37
Quality assurance	–	4	4
Finance and administration	1	33	34
Total	<u>3</u>	<u>144</u>	<u>147</u>

PRE-IPO SHARE OPTION SCHEME

Our Company has conditionally approved and adopted the Pre-IPO Share Option Scheme and the Share Option Scheme on 20 October 2011, the principal terms of which are summarised in the paragraph headed “Pre-IPO Share Option Scheme” in Appendix V to this prospectus.

Pursuant to the Pre-IPO Share Option Scheme, eligible participants of the scheme (including our Directors, senior management, consultants and other employees of our Group) may be granted options which entitle them to subscribe for Shares representing (when aggregated with options granted under any other scheme) a maximum of 10% of the issued share capital of our Company as of the Listing Date. As of the Latest Practicable Date, we have granted options to subscribe for 1,300,000 Shares pursuant to the Pre-IPO Share Option Scheme at an exercise price of 80% of the Placing Price to 10 participants (including 1 executive Director and 4 members of the senior management of our Group). All the options under the Pre-IPO Share Option Scheme were granted on 20 October 2011 and no further options will be granted under the Pre-IPO Share Option Scheme prior to the Listing Date. Each grantee of our Group paid HK\$10.00 as consideration for grant of the options. For details, please refer to the paragraph headed “Pre-IPO Share Option Scheme” in Appendix V to this prospectus.

DIRECTORS, SENIOR MANAGEMENT AND STAFF

SHARE OPTION SCHEME

The Company has conditionally adopted the Share Option Scheme on 20 October 2011. The purpose of the scheme is to give the participants the opportunity to obtain equity interest in our Company, thus providing them with the incentive to work for the best interest of our Group. As at the Latest Practicable Date, no share option has been granted pursuant to the Share Option Scheme. The principal terms of the Share Option Scheme are set out in the section headed “Share Option Scheme” in Appendix V of this prospectus.

BOARD COMMITTEES

Audit committee

We have established an audit committee on 20 October 2011 in compliance with Rule 5.28 of the GEM Listing Rules. The audit committee has adopted the written terms of reference in compliance with paragraph C3.3 of the Code on Corporate Governance Practices as set out in Appendix 15 to the GEM Listing Rules. The primary duties of the audit committee are to review the quarterly, half-yearly and annual reports, make recommendation as to the appointment and removal of external auditors, review and oversee the financial reporting process and internal control system of our Group. As at the Latest Practicable Date, the audit committee consisted of three members comprising Mr. Wong Yiu Kit, Mr. Tam Yuk Sang, Sammy and Mr. Kong Hing Ki, all of whom are independent non-executive Directors. Mr. Wong Yiu Kit is the chairman of the audit committee.

Remuneration committee

We have established a remuneration committee on 20 October 2011. The remuneration committee has adopted the written terms of reference in compliance with paragraph B1.1 of the Code on Corporate Governance Practices as set out in Appendix 15 to the GEM Listing Rules. The primary duties of the remuneration committee are to make recommendations to the Board on the overall remuneration policy and structure relating to all Directors and senior management of our Group, review and determine the terms of remuneration package, bonuses and other compensation payable to Directors and senior management. As at the Latest Practicable Date, the remuneration committee consisted of three members comprising Mr. Wong Yiu Kit, Mr. Tam Yuk Sang, Sammy and Mr. Kong Hing Ki, all of whom are independent non-executive Directors. Mr. Kong Hing Ki is the chairman of the remuneration committee.

Nomination committee

We have established a nomination committee on 20 October 2011. The nomination committee has adopted the written terms of reference in compliance with paragraph A4.4 of the Code on Corporate Governance Practices as set out in Appendix 15 to the GEM Listing Rules. The primary duties of the nomination committee are to make recommendations to the Board on appointment and re-appointment of Directors, and the management of our Board succession. As at the Latest Practicable Date, the nomination committee consisted of three members comprising Mr. Wong Yiu Kit, Mr. Tam Yuk Sang, Sammy and Mr. Kong Hing Ki, all of whom are independent non-executive Directors. Mr. Tam Yuk Sang, Sammy is the chairman of the nomination committee.

DIRECTORS, SENIOR MANAGEMENT AND STAFF

COMPLIANCE ADVISER

We have appointed Shenyin Wanguo as our compliance adviser in accordance with Rule 6A.19 of the GEM Listing Rules. Pursuant to Rule 6A.23 of the GEM Listing Rules, we will seek advice from the compliance adviser on a timely basis in the following circumstances:

- before the publication of any regulatory announcement, circular or financial report;
- where a transaction, which might be a notifiable or connected transaction, is contemplated including share issues and share repurchases;
- where we propose to use the proceeds of the Placing in a manner different from that detailed in this prospectus or where our business activities, developments or results deviate from any forecast, estimate, or other information in this prospectus; and
- where the Stock Exchange makes an inquiry of our Group regarding unusual movements in the price or trading volume of our Shares.

The terms of the appointment shall commence on the Listing Date and end on the date which we distribute our annual report of our financial results for the second full financial year commencing after the Listing Date and such appointment may be subject to extension by mutual agreement.

FUTURE PLANS AND PROSPECTS

BUSINESS OBJECTIVE AND STRATEGIES

Our Group has obtained the Tobacco Production Licence under which we are permitted to manufacture, sell and provide maintenance, overhaul as well as modification services in respect of casing and flavouring systems, feeding systems and PP systems. We have accumulated years of experience in the PRC tobacco machinery industry and have established good relationship with cigarette manufacturers and tobacco redrying factories in the PRC. We have also built up good reputation in terms of the quality of our products and services provided. Our Group aims to leverage on our competitive strengths and strive to become one of the leading tobacco machinery manufacturers in the PRC.

To achieve our business objective, we intend to adopt the following principal strategies:

Continuous product development and innovation

During the Track Record Period, we successfully developed a set of casing and flavouring system employing automatic mechanical devices in the storage, retrieval and feeding of semi-processed flavour and casing mixtures for the blending process, and secured a sales contract to supply this system to a cigarette manufacturer in Shanghai. We have also been engaged to design an automated casing and flavouring system with movable tanks, performing the function of a central blending centre, for a cigarette manufacturer in Kunming. Our Directors believe our Group's competitive edge lies in our strong development and customisation capabilities. It is our Group's objective to focus our design and development initiatives on the expansion of product range and to create new and enhanced series of catalogued special-purpose tobacco machinery products with innovative designs to meet the evolving requirements of cigarette manufacturers and tobacco redrying factories.

We plan to design a new casing and flavouring system equipping the operating features of movable tanks and automated storage, retrieval and feeding devices. In addition, we plan to continue our development with Nanjing University of Science and Technology of a new type of spraying device to be equipped with our casing and flavouring system. Such device aims to allow the spraying of casing and flavours in a more evenly manner, so as to enhance the taste and texture standardisation of individual cigarettes.

For our PP system, we plan to develop a new set of system employing two compressors. Currently, the PP system is equipped with one compressor with a maximum processing capability of approximately 12,000 kilograms of tobacco leaves per hour or 50 carton boxes per hour. In order to increase our Group's competitiveness, and more importantly, to cope with the technological advancement of our customers in their production line, we intend to develop a new PP system with processing capability of approximately 14,000 kilograms of tobacco leaves per hour or 70 carton boxes per hour.

As regards our PF system, we plan to develop a new set of system with only one tube connecting to one cigarette wrapping machine, and with a higher delivery capacity as compared to the existing system of up to 750 kilograms of processed cut tobacco per hour. Our Directors expect the new system will be able to meet the increasing demand of cigarette manufacturers of producing smaller quantity of individual cigarette brands and cater to the recent change in cigarette production line setting. Such one to one connection can also eliminate the need to clean up the pipe upon switching of production of different cigarette brands.

FUTURE PLANS AND PROSPECTS

We also intend to expand our scope of catalogued special-purpose tobacco machinery products and launch two research and development programs related to the development of (i) tobacco bale slicer designed for use by the cigarette manufacturers in slicing unwrapped tobacco bale into slices of required sizes for subsequent tobacco processing; and (ii) tobacco redrying system designed for use by tobacco redrying factories in the redrying process.

In order to strengthen our research and development capabilities to cope with our continuous product development and innovation, we intend to recruit additional technical staff for project design and product development. In addition, we may enter into cooperation agreements with other academic institutes for the joint development of new products.

Enhancing corporate profile and increasing market penetration

Our Group intends to enhance corporate profile through employing multi-faceted advertising strategies. We will promote our corporate image through advertising on tobacco magazines and participating in trade exhibitions in the PRC. In addition, we will put more efforts in promoting our Group and our products in the PRC through sending out corporate and product brochures as well as video compact discs. We also plan to put more efforts in marketing activities to enhance our market penetration in the PRC. Our Group will hold seminars and organise product launch campaigns to introduce our products and services to our existing and potential customers. At the same time, by establishing close contacts with the cigarette manufacturers and tobacco redrying factories, our Group will be able to keep abreast of market information and take appropriate measures to meet customers' requirements. We will rely on the above strategies to maintain our competitive position and together with the efforts put in marketing and advertising activities as mentioned above, our Directors are confident that our Group will be able to increase its market share and attract new customers.

Enhancing production processing capabilities

We are committed to designing and manufacturing products with high quality standards. Apart from employing competent and experienced personnel to carry out our quality control and assurance procedures, our Directors believe that it is vital to deploy advanced and reliable machinery and equipment in the production of our customised products. We intend to purchase more production processing equipment with digital control or automation to enhance the stability of our product quality. In addition, to cope with our business development, we intend to upgrade the facilities at our existing production base, including the water and electricity supply systems as well as the steam and compressed air supply system used mainly for the testing of pumps, valves and pipe connection of our semi-finished products. We also plan to set up an automated surface painting system to reduce the processing time and improve the quality of our products.

Strengthening management information system

Generally, we secure our sales contracts through submitting proposals to project owners or tenders to tendering companies. Hence, it is of vital importance that we evaluate the cost to completion before submission of proposals and tenders since the bidding price is one of the selection criteria. Moreover, as our Group conducts business on a project basis, we have to conduct regular review on the project status and up-to-date cost analysis. Currently, although all the cost information is provided

FUTURE PLANS AND PROSPECTS

to management for decision making and evaluation, it is not on a real time basis and require certain manual processing. As such, we plan to upgrade our management information system so as to keep pace with the business development of our Group.

IMPLEMENTATION PLANS

Our Directors have drawn up an implementation plan with respect to our Group's operations for the period from the Latest Practicable Date to 31 December 2013 to achieve our business objective along with the strategies. The implementation plan is based on certain bases and assumptions as set out in the paragraph headed "Bases and assumptions" in this section which are inherently subject to uncertainties and unpredictable factors. Therefore, there is no assurance that our Group's business plan will materialise in accordance with the estimated time frame or even be accomplished at all. Our Directors will use their best endeavours to anticipate future changes in the market, take measures and be flexible so that our Group may stay ahead of or react timely and appropriately to such changes.

1. Continuous product development and innovation

From the Latest Practicable Date to 31 December 2011	From 1 January 2012 to 30 June 2012	From 1 July 2012 to 31 December 2012	From 1 January 2013 to 30 June 2013	From 1 July 2013 to 31 December 2013
Design and develop new PP system	Design and develop new PP system	Design and develop new PP system	Design and develop new casing and flavouring system	Design and develop new casing and flavouring system
Design and develop new spraying device	Design and develop new spraying device	Design and develop new spraying device	Design and develop new PF system	Design and develop tobacco redrying system
Recruit additional technical staff for project design and product development	Design and develop new casing and flavouring system	Design and develop new casing and flavouring system	Design and develop tobacco bale slicers	Recruit additional technical staff for project design and product development
	Design and develop tobacco bale slicers	Design and develop new PF system	Design and develop tobacco redrying system	
	Recruit additional technical staff for project design and product development	Design and develop tobacco bale slicers	Recruit additional technical staff for project design and product development	
		Design and develop tobacco redrying system		
		Recruit additional technical staff for project design and product development		
Amount to be applied from the net proceeds of the Placing:				
HK\$1,364,000	HK\$5,694,000	HK\$9,542,000	HK\$13,353,000	HK\$3,760,000

FUTURE PLANS AND PROSPECTS

2. Enhancing corporate profile and increasing market penetration

From the Latest Practicable Date to 31 December 2011	From 1 January 2012 to 30 June 2012	From 1 July 2012 to 31 December 2012	From 1 January 2013 to 30 June 2013	From 1 July 2013 to 31 December 2013
Post advertisement in tobacco magazines	Post advertisement in tobacco magazines	Post advertisement in tobacco magazines	Post advertisement in tobacco magazines	Post advertisement in tobacco magazines
	Design and distribute corporate and product brochures as well as video compact discs	Organise product launch promotional activities for casing and flavouring systems	Design and distribute product brochures and video compact discs	Design and distribute product brochures and video compact discs
	Participate in trade exhibitions		Participate in trade exhibitions	Organise promotional activities for existing and new products
			Organise promotional activities for existing and new products	

Amount to be applied from the net proceeds of the Placing:

HK\$18,000	HK\$156,000	HK\$1,276,000	HK\$1,040,000	HK\$1,210,000
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3. Enhancing production processing capabilities

From the Latest Practicable Date to 31 December 2011	From 1 January 2012 to 30 June 2012	From 1 July 2012 to 31 December 2012	From 1 January 2013 to 30 June 2013	From 1 July 2013 to 31 December 2013
Purchase machinery and equipment	Purchase machinery and equipment	Purchase machinery and equipment	Purchase machinery and equipment	Purchase machinery and equipment
		Upgrade production facilities		

Amount to be applied from the net proceeds of the Placing:

HK\$480,000	HK\$960,000	HK\$1,500,000	HK\$670,000	HK\$1,220,000
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FUTURE PLANS AND PROSPECTS

The following table sets forth the types of machinery and equipment to be purchased by our Group to enhance our production processing capabilities:

Types of machinery and equipment	<i>HK\$'000</i>
CNC shearing machine	840
CNC press brake	480
Automatic pipe welding machine	480
CNC lathes	670
Turret punch machine	800
Hydraulic press machine	540
Water and electricity system	360
Steam and compressed air supply system	660
	660
 Total	 4,830

4. Strengthening management information system

From the Latest Practicable Date to 31 December 2011	From 1 January 2012 to 30 June 2012	From 1 July 2012 to 31 December 2012	From 1 January 2013 to 30 June 2013	From 1 July 2013 to 31 December 2013
Evaluate, acquire and implement management information system	-	-	-	-

Amount to be applied from the net proceeds from the Placing:

HK\$480,000	-	-	-	-
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FUTURE PLANS AND PROSPECTS

BASES AND ASSUMPTIONS

The business objectives set out by our Directors are based on the following bases and assumptions:

- there will be no significant economic change in respect of inflation, interest rate, tax rate and currency exchange rate in the PRC, Hong Kong or any part of the world that will adversely affect the business of our Group;
- our Group will have sufficient financial resources to meet the planned capital expenditure and business development requirements during the period to which the business objectives relate;
- there will be no material change in the existing laws (whether in the PRC, Hong Kong or any part of the world), policies or industry or regulatory treatments relating to our Group, or in the political, economic or market conditions in which our Group operates;
- there will be no change in the funding requirement for each of the scheduled achievements as outlined under the paragraph headed “Implementation plans” in this section;
- there will be no material change in the bases or rates of taxation applicable to our Group;
- there will be no disaster, natural, political or otherwise, which would materially disrupt the business or operation of our Group or cause substantial loss, damage or destruction to our property or facilities;
- there will be no change in the effectiveness of the licences, permits and registration held by our Group; and
- our Group will not be materially affected by the risk factors as set out under the section headed “Risk factors” in the prospectus.

FUTURE PLANS AND PROSPECTS

REASONS FOR THE PLACING AND USE OF PROCEEDS

Our Directors believe that the Listing will enhance our Group's profile, enhance our capital base and provide additional working capital to implement the future plans as set out in the paragraphs headed "Business objective and strategies" and "Implementation plans" in this section.

The net proceeds from the Placing based on the Placing Price of HK\$1.20 per Share (being the mid-point of the stated range of the Placing Price), after deducting the underwriting fees and other expenses, are estimated to be approximately HK\$47.3 million. Our Directors intend to apply the aforesaid net proceeds in the following manner:

	From the Latest Practicable Date to		For the six months ending			Total
	31 December 2011	30 June 2012	31 December 2012	30 June 2013	31 December 2013	
	(HK\$'000)	(HK\$'000)	(HK\$'000)	(HK\$'000)	(HK\$'000)	(HK\$'000)
Continuous product development and innovation	1,364	5,694	9,542	13,353	3,760	33,713
Enhancing corporate profile and increasing market penetration	18	156	1,276	1,040	1,210	3,700
Enhancing production processing capabilities	480	960	1,500	670	1,220	4,830
Strengthening management information system	480	-	-	-	-	480
	<u>2,342</u>	<u>6,810</u>	<u>12,318</u>	<u>15,063</u>	<u>6,190</u>	<u>42,723</u>

The balance of approximately HK\$4.6 million will be applied towards additional general working capital of our Group.

During the Track Record Period, our total product research and development expenditures amounted to approximately HK\$246,000, HK\$394,000 and HK\$717,000 respectively, which represented approximately 0.3%, 0.4% and 1.1% respectively of our total turnover. We believe that the users of our products, being mainly cigarette manufacturers in the PRC, are focused on continuous technological improvements in their cigarette production process. As a result, in order to maintain our competitiveness, our Directors intend to apply approximately 71.2% of the above net proceeds on continuous product development and innovation, despite the small amounts of product research and development expenditures recorded during the Track Record Period. We plan to expand our product range and create new and enhanced series of catalogued special-purpose tobacco machinery products with innovative designs to meet the evolving requirements of cigarette manufacturers and tobacco redrying factories. We also intend to expand our scope of catalogued special-purpose tobacco machinery products and launch two

FUTURE PLANS AND PROSPECTS

research and development programs related to the development of (i) tobacco bale slicer designed for use by the cigarette manufacturers in slicing unwrapped tobacco bale into slices of required sizes for subsequent tobacco processing; and (ii) tobacco redrying system designed for use by tobacco redrying factories in the redrying process. We intend to use the above net proceeds from the Placing of HK\$33,713,000 on continuous product development and innovation as follows:

- approximately HK\$10,883,000 for designing and producing prototypes of a new casing and flavouring system equipping the operating features of movable tanks and automated storage, retrieval and feeding devices comprising the costs of materials, parts, components and toolings;
- approximately HK\$4,340,000 for designing and producing prototypes of a new type of spraying device comprising the costs of materials, parts, components and toolings;
- approximately HK\$4,500,000 for developing and producing prototypes of a new set of PP system employing two compressors comprising the costs of materials, parts, components and toolings;
- approximately HK\$680,000 for developing and producing prototypes of a new set of PF system with only one tube connecting to one cigarette wrapping machine and with a higher delivery capacity as compared to the existing system;
- approximately HK\$4,780,000 and HK\$7,230,000 for developing and producing prototypes of tobacco bale slicer and tobacco redrying system respectively comprising the costs of materials, parts, components and toolings; and
- approximately HK\$1,300,000 for recruiting additional technical staff for project design and product development.

Apart from applying the net proceeds from the Placing of approximately HK\$4,830,000 on the purchase of machinery and equipment to enhance our production processing capabilities, details of which are disclosed in the paragraph headed “Implementation plans – 3. Enhancing production processing capabilities” in this section, our Directors do not plan to use the net proceeds on capital expenditures for continuous product development and innovation.

Our Directors consider that the net proceeds from the Placing of approximately HK\$47.3 million will be sufficient to finance our Group’s business plans up to the year ending 31 December 2013.

To the extent that the net proceeds from the issue of the Placing Shares are not immediately required for the above purpose, it is the present intention of our Directors that such proceeds will be placed on short-term interest bearing deposits with authorised financial institutions.

CONTROLLING SHAREHOLDERS AND SUBSTANTIAL SHAREHOLDERS

SUBSTANTIAL SHAREHOLDERS

So far as our Directors are aware, immediately following the completion of the Placing and the Capitalisation Issue (but without taking into account any Shares which may be allotted and issued pursuant to the exercise of options granted under the Pre-IPO Share Option Scheme and the Share Option Scheme), the following persons will have an interest or short position in the Shares or underlying Shares which would fall to be disclosed to our Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or, will be directly or indirectly interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of our Group:

Name	Capacity	Number of Shares	Approximate percentage of shareholding immediately following the Capitalisation Issue and the Placing
LinkBest ⁽¹⁾	Beneficial owner	90,000,000	45%
Open Venture ⁽²⁾	Beneficial owner	60,000,000	30%
Mr. Wei ⁽³⁾	Interest of a controlled corporation and family interest	150,000,000	75%
Ms. Liu ⁽⁴⁾	Interest of a controlled corporation and family interest	150,000,000	75%

Notes:

1. LinkBest is wholly owned by Mr. Wei.
2. Open Venture is wholly owned by Ms. Liu.
3. Mr. Wei is the sole shareholder of LinkBest which is interested in 90,000,000 Shares and as the spouse of Ms. Liu, he is deemed to be interested in 60,000,000 Shares held by Open Venture, being a corporation wholly owned by Ms. Liu.
4. Ms. Liu is the sole shareholder of Open Venture which is interested in 60,000,000 Shares and as the spouse of Mr. Wei, she is deemed to be interested in 90,000,000 Shares held by LinkBest, being a corporation wholly owned by Mr. Wei.

CONTROLLING SHAREHOLDERS AND SUBSTANTIAL SHAREHOLDERS

CONTROLLING SHAREHOLDERS

So far as our Directors are aware, immediately following completion of the Placing and the Capitalisation Issue (but without taking into account any Shares which may be allotted and issued pursuant to the exercise of options that have been granted under the Pre-IPO Share Option Scheme or may be granted under the Share Option Scheme), the following persons individually and/or collectively are entitled to exercise or control the exercise of 30% or more of the voting power at the general meetings of our Company or who is or are in a position to control the composition of a majority of our Board and are therefore regarded as Controlling Shareholders under the GEM Listing Rules:

Name	Capacity	Number of Shares	Approximate percentage of shareholding immediately following the Capitalisation Issue and the Placing
LinkBest ⁽¹⁾	Beneficial owner	90,000,000	45%
Open Venture ⁽²⁾	Beneficial owner	60,000,000	30%
Mr. Wei ⁽³⁾	Interest of a controlled corporation and family interest	150,000,000	75%
Ms. Liu ⁽⁴⁾	Interest of a controlled corporation and family interest	150,000,000	75%

Notes:

1. LinkBest is wholly owned by Mr. Wei.
2. Open Venture is wholly owned by Ms. Liu.
3. Mr. Wei is the sole shareholder of LinkBest which is interested in 90,000,000 Shares and as the spouse of Ms. Liu, he is deemed to be interested in 60,000,000 Shares held by Open Venture, being a corporation wholly owned by Ms. Liu.
4. Ms. Liu is the sole shareholder of Open Venture which is interested in 60,000,000 Shares and as the spouse of Mr. Wei, she is deemed to be interested in 90,000,000 Shares held by LinkBest, being a corporation wholly owned by Mr. Wei.

CONTROLLING SHAREHOLDERS AND SUBSTANTIAL SHAREHOLDERS

INDEPENDENCE FROM CONTROLLING SHAREHOLDERS

Our Directors consider that our Group is capable of carrying on its business independently of our Controlling Shareholders and their associates taking into account the following factors.

Operational independence

Our Group holds all relevant licences necessary to carry on our business, and have the capability in terms of capital, equipment, workforce, raw material sourcing and sales and marketing to operate our business independently from our Controlling Shareholders and their associates.

Save for the continuing connected transactions as disclosed in the paragraph headed “Continuing connected transactions exempt from reporting, annual review, announcement and independent shareholders’ approval requirements” in the section headed “Connected transactions” in this prospectus in respect of (i) the purchase and sale of switchgear, control switchbox and working platform between our Group and Longtai and provision of subcontracting work from Longtai to our Group; and (ii) lease of the Baoying Renheng office premises to Longtai and Jinchuang after Listing, our Directors do not expect that there will be any other transactions between our Group and the Controlling Shareholders or their associates upon or shortly after Listing. Our Directors estimate that the annual aggregate values of each type of the said continuing connected transactions will not exceed HK\$1 million for the three years ending 31 December 2013. In addition, our Directors are of the view that the goods supplied by Longtai can be easily sourced from other suppliers on similar terms as provided by Longtai. Accordingly, our Directors do not consider that our Group is in any way dependent on our Controlling Shareholders and their associates for any part of our operations.

Management independence

Our business and the business of our Controlling Shareholders are managed and operated by different management teams. The management and operational decisions of our Group are made by our Directors and senior management. Our Board consists of three executive Directors and three independent non-executive Directors. We believe that our independent non-executive Directors will be able to exercise their independent judgment and provide impartial opinion in the decision making process of our Board to protect the interests of the Shareholders. Our Directors are of the view that our Group is capable of managing its business separately and independently from the business of our Controlling Shareholders.

Financial independence

As at the Latest Practicable Date, there was no financing arrangement between our Group and our Controlling Shareholders and their associates. The outstanding amount of HK\$2.5 million payable by our Group to Grand Bright as of 31 December 2010 was fully settled prior to the Latest Practicable Date. In addition, our Group does not share any banking or credit facilities with our Controlling Shareholders or their associates. Furthermore, our accounting system as well as our

CONTROLLING SHAREHOLDERS AND SUBSTANTIAL SHAREHOLDERS

accounting and finance team is independent from those of our Controlling Shareholders. In view of the above, our Directors consider that our Group is capable of maintaining financial independence from our Controlling Shareholders.

NON-COMPETITION UNDERTAKING

In order to eliminate any existing and future competing business with our Group, LinkBest, Open Venture, Mr. Wei and Ms. Liu (collectively the “Covenantors”) which are also our substantial shareholders, have entered into the Non-Competition Undertaking dated 20 October 2011 with our Group, pursuant to which the Covenantors shall not and shall procure their associates (other than members of our Group) not to engage or involve in any business which may compete with the business of our Group.

The Covenantors’ obligations under this undertaking are conditional upon the conditions stated under the paragraph headed “Conditions of the Placing” in the section headed “Structure and conditions of the Placing” in this prospectus being fulfilled. If such conditions are not fulfilled on or before the date falling the 30th day after the date of this prospectus or such other date as the parties thereto may agree, this undertaking shall become null and void and cease to have effect. The Non-Competition Undertaking includes the following provisions:

- (A) The Covenantors undertake to our Company (for itself and for the benefit of the members of our Group) that they will not, and will procure that their associates will not engage or otherwise be involved in any business which competes or is likely to compete, either directly or indirectly, with any of the businesses carried on by any member(s) of our Group from time to time, including, but not limited to, design and manufacture of catalogued special-purpose tobacco machinery products, being the current principal business of our Group and any business which is in any respect will or may be in competition with the businesses conducted by the Group from time to time within Hong Kong or the PRC or any other parts of the world (the “**Restricted Business**”); provided that there shall be no restrictions on the Covenantors, jointly or severally, or their associates from:
 - (1) holding or being interested in any shares or other securities in any company which engages or involves in the Restricted Business, provided that such shares or securities are listed on a recognised stock exchange and either (a) the Restricted Business and assets relating thereto account for less than 10% of such listed company’s net profit after taxation, minority interests and exceptional/extraordinary items, as shown in such listed company’s latest audited consolidated accounts; or (b) the total number of the shares held by the Covenantors, jointly or severally, and their associates do not exceed 5% of such listed company’s issued share capital and provided further that at all times there is a shareholder holding more shares in the relevant listed company than the aggregate shareholding of the Covenantors and their associates; and

CONTROLLING SHAREHOLDERS AND SUBSTANTIAL SHAREHOLDERS

- (2) holding any Shares or other securities in our Company or any member of our Group.

- (B) The Covenantors further grant to our Company (for itself and for the benefits of the members of our Group) and will procure their associates to grant to our Company the first right of refusal regarding future business opportunities in relation to any of the Restricted Business and not to compete with our Group in any jurisdiction (the “**First Right of Refusal**”).

- (C) The Covenantors also undertake to make full disclosure of all relevant information and render such assistance and co-operation as are necessary for our Company to review comply and/or enforce this Non-Competition Undertaking.

- (D) The Covenantors agree that our Company may disclose, to any regulatory bodies or the public in any manner at its absolute discretion, decision on matters reviewed by its independent non-executive directors relating to the compliance and enforcement of the Non-competition Undertaking, including but not limited to the exercise of the First Right of Refusal.

- (E) The Covenantors undertake to abstain from the meeting and voting and not to be counted as quorum in any shareholders’ meetings of our Company, where there is actual and/or potential conflicting of interest.

- (F) The Covenantors represent and warrant that neither they nor any of their associates are currently interested or engaging, directly or indirectly, in (whether as a shareholder, director, partner, agent or otherwise and whether for profit, reward or otherwise) the Restricted Business otherwise than through our Group.

- (G) Each of the Covenantors undertakes to indemnify our Company from and against any and all losses, damages and costs (including legal expenses) which loss, damage or cost is resulted from any failure to comply with the terms of the Non-Competition Undertaking by the Covenantors or any of their respective associates and the Covenantors agree to repay our Company any benefit obtained from their failure to comply with the terms of the Non-Competition Undertaking. The indemnity therein contained shall be without prejudice to any other rights and remedies of our Company in relation to any such breach and all such other rights and remedies are expressly reserved by our Company.

The Non-Competition Undertaking shall cease to have any effect on the earliest of the date on which (i) our Company becomes a wholly-owned subsidiary of the Covenantors; (ii) the Covenantors (together with their associates) cease to hold, in aggregate, whether directly or indirectly, 10% or more of the issued share capital of our Company; or (iii) the Shares cease to be listed and traded on GEM.

CONTROLLING SHAREHOLDERS AND SUBSTANTIAL SHAREHOLDERS

On the other hand, Mr. Wei, one of the Covenantors, has since 1 August 2001 been appointed as a director of Hongta Renheng. Hongta Renheng produces high-grade Hongta brand coated cardboard (folding box board and solid bleached sulphate series: including but not limited to reeled board, sheeted board, inner frame board for cigarette packs, antibiotic coated cardboard, base board for liquid packaging board and anti-falsification coated cardboard with unique safety marking, with basis weights ranging from 170 to 400 g/m²) which is produced from imported wood pulp and chemical raw materials. Hongta Renheng's paper products have been widely used in the industries such as tobacco, medicine, food, cosmetics and daily necessities. Though Hongta Renheng produces coated cardboard for the use of tobacco packaging by cigarette manufacturers, those products are different from our tobacco packaging paper, namely the hot stamped foil, and there is no competition between the two. We have started trading tobacco packaging paper during the financial year ended 31 December 2010.

Mr. Wei has since 6 May 1994 been appointed as a director of HK Hongta. HK Hongta focuses on marketing the Hongta brand tobacco products into the international market and processing of air-cured tobacco in blend type cigarette. Though HK Hongta and our Group are in the same tobacco industry, the clienteles and business operations are different and there is no direct or indirect competition between the two.

None of the Covenantors had any interest in Hongta Renheng or HK Hongta as at the Latest Practicable Date.

As stated above, each of the Covenantors has provided the Non-Competition Undertaking to us with a view to eliminate any existing and future competing business with our Group. They have also undertaken to us that they shall provide all information necessary for us to enforce the Non-Competition Undertaking and to facilitate the annual review by the independent non-executive Directors.

INDEMNITIES

A deed of indemnity dated 20 October 2011, was executed by LinkBest, Open Venture, Mr. Wei and Ms. Liu to render, subject to certain exceptions, joint and several indemnities in favour of our Company in connection with, among other things, (a) any liability for Hong Kong estate duty which might be incurred by any member of our Group by virtue of any transfer of property (within the meaning of sections 35 and 43 of the Estate Duty Ordinance (Chapter 111 of the Laws of Hong Kong) or the equivalent thereof under the laws of any jurisdiction outside Hong Kong) to any member of our Group on or before the date on which the Placing becomes unconditional, and (b) any tax liabilities (including all fines, penalties, costs, charges, expenses and interest incidental or relating to taxation) which might be payable by any member of our Group in respect of any income, profits or gains earned, accrued or received or deemed to have been earned, accrued or received on or before the Listing Date whether alone or in conjunction with any other event, whenever occurring and whether or not the relevant taxation is chargeable against or attributable to any other person including any and all taxation resulting from the receipt by any member of our Group of any amount paid by the Indemnifiers under the deed of indemnity. Further details of the deed of indemnity are set out in the paragraph headed "Estate duty and tax indemnities" under the section headed "Other information" in Appendix V to this prospectus.

SHARE CAPITAL

SHARE CAPITAL

The share capital of our Company immediately following the completion of the Capitalisation Issue and the Placing is set out in the table below. The table is prepared on the basis of the Capitalisation Issue and the Placing becoming unconditional and the issue of Placing Shares pursuant thereto is made as described herein. It takes no account of any new Shares which may be allotted and issued pursuant to the exercise of any options granted under the Pre-IPO Share Option Scheme and any option which may be granted under the Share Option Scheme or of any Shares which may be allotted and issued or repurchased by our Company under the general mandates for the allotment and issue or repurchase of Shares granted to Directors as referred to below or otherwise.

HK\$

Authorised share capital:

<u>1,000,000,000</u>	Shares	<u>10,000,000</u>
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Issued and to be issued, fully paid or credited as fully paid

100	Shares in issue as at the Latest Practicable Date	1
149,999,900	Shares to be issued pursuant to the Capitalisation Issue	1,499,999
<u>50,000,000</u>	Placing Shares to be issued pursuant to the Placing	<u>500,000</u>

Total

<u>200,000,000</u>	Shares	<u>2,000,000</u>
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Minimum public float

Pursuant to Rule 11.23(7) of the GEM Listing Rules, at least 25% of the total issued share capital of our Company must at all times be held by the public. The 50,000,000 Placing Shares represent 25% of the issued share capital of our Company upon Listing.

RANKING

The Placing Shares will rank pari passu in all respects with all other Shares now in issue or to be allotted and issued and will qualify for all dividends or other distributions declared, made or paid after the date of this prospectus.

PRE-IPO SHARE OPTION SCHEME AND SHARE OPTION SCHEME

Our Company has conditionally adopted the Pre-IPO Share Option Scheme and the Share Option Scheme, the major terms of which are set out in the sections headed “Pre-IPO Share Option Scheme” and “Share Option Scheme” in Appendix V to this prospectus, respectively.

SHARE CAPITAL

GENERAL MANDATE TO ISSUE SHARES

Subject to the Placing becoming unconditional, the Directors have been granted a general unconditional mandate to allot and issue and deal with the unissued Shares with an aggregate nominal value of not more than the sum of:

- (a) 20% of the aggregate nominal value of the share capital of our Company in issue immediately following the completion of the Capitalisation Issue and the Placing (not including Shares which may be allotted and issued pursuant to the exercise of the options granted under the Pre-IPO Share Option Scheme and any option which may be granted under the Share Option Scheme); and
- (b) the aggregate nominal value of the share capital of our Company repurchased by our Company (if any) pursuant to the general mandate to repurchase Shares as described below.

Our Directors may, in addition to the Shares which they are authorised to issue under the mandate, allot, issue and deal in the Shares pursuant to a rights issue, open offer, an issue of Shares pursuant to the exercise of subscription rights attaching to any warrants of our Company, scrip dividends or similar arrangements or the options granted under the Pre-IPO Share Option Scheme and any option which may be granted under the Share Option Scheme or similar arrangement for the time being adopted.

GENERAL MANDATE TO REPURCHASE SHARES

Subject to the Placing becoming unconditional, our Directors have been granted a general unconditional mandate to exercise all the powers of our Company to repurchase Shares with a total nominal value of not more than 10% of the aggregate nominal value of the share capital of our Company in issue following the completion of the Capitalisation Issue and the Placing (not including Shares which may be allotted and issued pursuant to the exercise of the options granted under the Pre-IPO Share Option Scheme and any option which may be granted under the Share Option Scheme).

This mandate only relates to repurchases made on the Stock Exchange, or on any other stock exchange on which the Shares are listed (and which is recognised by the SFC and the Stock Exchange for this purpose), and such repurchases are made in accordance with all applicable laws and the requirements of GEM Listing Rules. A summary of the relevant GEM Listing Rules is set out in the paragraph headed “Repurchase by the Company of its own securities” under the section headed “Further information about the Company and its subsidiaries” in Appendix V to this prospectus.

STRUCTURE AND CONDITIONS OF THE PLACING

PRICE PAYABLE ON SUBSCRIPTION

The Placing Price plus a 1% brokerage fee, a 0.003% SFC transaction levy and a 0.005% Stock Exchange trading fee make up total price payable in cash on subscription.

CONDITIONS OF THE PLACING

The Placing will be conditional upon, among others:

- (i) the Stock Exchange granting the listing of, and permission to deal in, the Shares in issue and the Shares to be issued as mentioned herein on GEM;
- (ii) the agreement on the Placing Price between the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) being entered into on or before the Price Determination Date; and
- (iii) the obligations of the Underwriter under the Underwriting Agreement becoming unconditional (including the waiver of any condition(s) by Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) and not being terminated in accordance with the terms of that agreement or otherwise),

in each case, on or before the dates and times specified in the Underwriting Agreement (unless and to the extent such conditions are validly waived on or before such dates and times) and in any event not later than 27 November, 2011, being the date which is the 30th day after the date of this prospectus.

If such conditions have not been fulfilled or waived prior to the times and dates specified, the Placing will lapse, all money received will be refunded to applicants of the Placing without interest and the Stock Exchange will be notified immediately. Notice of the lapse of the Placing will be published by the Company on the GEM website at www.hkgem.com and the Company's website at www.renhengenterprise.com on the next business day following such lapse.

THE PLACING

50,000,000 Placing Shares are being offered pursuant to the Placing, representing in aggregate 25% of the enlarged issued share capital of the Company.

The Placing is fully underwritten by the Underwriter (subject to the terms and conditions of the Underwriting Agreement). Pursuant to the Placing, it is expected that the Underwriter, on behalf of the Company, will conditionally place 50,000,000 Placing Shares at the Placing Price to selected individual, professional and institutional investors in Hong Kong. Professional and institutional investors generally include brokers, dealers, companies, high net worth individuals and companies (including fund managers) whose ordinary business involves dealings in shares and other securities and corporate entities which regularly invest in shares and other securities.

STRUCTURE AND CONDITIONS OF THE PLACING

BASIS OF ALLOCATION

Allocation of the Placing Shares to selected individual, professional and institutional investors will be based on a number of factors, including the level and timing of demand and whether or not it is expected that the relevant investors are likely to purchase further Shares or hold or sell their Shares after the Listing. Such allocation is intended to result in a distribution of the Placing Shares which would lead to the establishment of a solid professional and institutional shareholder base to the benefit of the Company and the Shareholders as a whole. In particular, the Placing Shares will be allocated pursuant to Rule 11.23(8) of the GEM Listing Rules, that not more than 50% of the Shares in public hands at the time of Listing will be owned by the three largest public Shareholders.

No allocations will be permitted to nominee companies unless the name of the ultimate beneficiary is disclosed, without the prior written consent of the Stock Exchange. There will not be any preferential treatments in the allocation of the Placing Shares to any persons. Details of the Placing will be announced in accordance with Rules 10.12(4), 16.08 and 16.16 of the GEM Listing Rules.

COMMENCEMENT OF DEALINGS

Dealings in the Shares on GEM are expected to commence at 9:00 a.m. on 18 November 2011. The Shares will be traded in board lots of 2,000 Shares each.

SHARES WILL BE ELIGIBLE FOR ADMISSION INTO CCASS

If the Stock Exchange grants the listing of and permission to deal in the Shares in issue and to be issued as mentioned in this prospectus on GEM and the Company complies with the stock admission requirements of HKSCC, the Shares will be accepted as eligible securities by HKSCC for deposit, clearance and settlement in CCASS with effect from the date of commencement of dealings in the Shares on GEM or any other date as determined by HKSCC. Settlement of transactions between participants of the Stock Exchange is required to take place in CCASS on the second business day after any trading day.

All necessary arrangements have been made for the Shares to be admitted into CCASS.

All activities under CCASS are subject to the General Rules of CCASS and CCASS Operational Procedures in effect from time to time.

In respect of the dealings in the Shares which may be settled through CCASS, investors should seek the advice of their stockbroker or other professional adviser for details of those settlement arrangements and how such arrangements will affect their rights and interests.

PLACING PRICE

The Placing Price is expected to be fixed by agreement between the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) on or before the Price Determination Date, which is currently scheduled on 9 November 2011 (or such later date as agreed between the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter)).

STRUCTURE AND CONDITIONS OF THE PLACING

If the Company and Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) are unable to reach an agreement on the Placing Price by the Price Determination Date, the Placing will not become unconditional and will not proceed. In such event, the Company will issue an announcement on the GEM website at www.hkgem.com and the Company's website at www.renhengenterprise.com.

The Placing Price will not be more than HK\$1.30 per Placing Share and is currently expected to be not less than HK\$1.10 per Placing Share. Subscribers, when subscribing for the Shares, shall pay the Placing Price plus 1% brokerage, 0.005% Stock Exchange trading fee and 0.003% SFC transaction levy. Assuming the Placing Price of HK\$1.30 or HK\$1.10 per Share (being the highest and lowest points of indicative Placing Price range respectively), investors shall pay HK\$2,626.21 or HK\$2,222.18 for every board lot of 2,000 Shares, respectively. The Placing Price will fall within the indicative Placing Price range as stated in this prospectus unless otherwise announced, as further explained below.

The Placing Price and the level of indication of interest in the Placing are expected to be announced on the GEM website at www.hkgem.com and our Company's website at www.renhengenterprise.com on or before 17 November 2011.

If, based on the level of indication of interest expressed by prospective institutional, professional or other investors during the book-building process, Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) consider it appropriate, and with the consent of the Company, the indicative Placing Price range may be reduced below that stated in this prospectus at any time on or before the Price Determination Date. In such a case, the Company will, as soon as practicable following the decision to make such reduction, cause to be published on the GEM website at www.hkgem.com and our Company's website at www.renhengenterprise.com an announcement of such change on or before the Price Determination Date. In the absence of any announcement being published on the GEM website and our Company's website of a reduction in the indicative Placing Price range stated in this prospectus in the manner set out herein, the Placing Price, upon agreement by Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) and the Company, will under no circumstances be set outside the indicative Placing Price range as stated in this prospectus.

UNDERWRITING

UNDERWRITER

Shenyin Wanguo Capital (H.K.) Limited

UNDERWRITING ARRANGEMENTS

Underwriting Agreement

In connection with the Placing, the Company has entered into the Underwriting Agreement, amongst other parties, with the Underwriter. Under the Underwriting Agreement, subject to the conditions set out therein, the Underwriter would agree to procure subscribers for, or failing which, to itself subscribe as principal for, the Placing Shares being offered pursuant to the Placing.

Pursuant to the Underwriting Agreement, the Company is offering the Placing Shares for subscription by way of Placing at the Placing Price, on and subject to the terms and conditions in the Underwriting Agreement and this prospectus.

Subject to, among other conditions, the Stock Exchange granting the listing of, and permission to deal in, the Shares in issue and to be issued as mentioned in this prospectus on or before the 30th day after the date of this prospectus and satisfaction or waiver of certain other conditions set out in the Underwriting Agreement, the Underwriter would agree to subscribe for or procure subscribers for the Placing Shares on the terms and conditions of the Placing.

Grounds for termination

Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) is entitled, upon giving a written notice to the Company to terminate the Underwriting Agreement if any of the following events occur at any time prior to 8:00 a.m. (Hong Kong time) on the Listing Date (which is expected to be on 18 November 2011):

- (a) if there has come to the notice of the Lead Manager:–
 - (i) that any statement, considered by Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) to be material, contained in any of the placing documents in relation to the Placing was when the same was issued, or has become, untrue, incorrect or misleading in any material respect; or
 - (ii) that any matter has arisen or has been discovered which would, had it arisen or been discovered immediately before the date of this prospectus, constitute an omission therefrom considered by the Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) to be material to the Placing; or
 - (iii) any breach of any of the obligations imposed upon any party to the Underwriting Agreement (other than Shenyin Wanguo); or

UNDERWRITING

- (iv) any change or development involving a prospective change in the conditions, business affairs, prospects or the financial or trading position of the Group as a whole; or
 - (v) any breach, reasonably considered by the Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) to be material, of any of the warranties of the Underwriting Agreement;
- (b) there shall develop, occur, exist or come into effect:–
- (i) any new law or regulation or any change or development involving a prospective change in existing laws or regulations or any change or development involving a prospective change in the interpretation or application thereof by any court or other competent authority of the Cayman Islands, the PRC, Hong Kong, the BVI, or any other relevant jurisdiction; or
 - (ii) any change or development involving a prospective change, or any event or series of events likely to result in any change or development involving a prospective change in local, national or international, financial, political, military, industrial, economic, currency market, fiscal or regulatory or market conditions or any monetary or trading settlement system (including but not limited to conditions in stock and bond markets, money and foreign exchange markets and inter-bank markets) in or affecting the Cayman Islands, the PRC, Hong Kong, the BVI, or any other relevant jurisdiction; or
 - (iii) any suspension or limitation on trading in shares or securities generally on the Stock Exchange, or minimum or maximum prices for trading having been fixed, or maximum ranges for prices having been required, by any of the said exchange or by such system or by order of any regulatory or governmental authority, or if a disruption has occurred in securities settlement or clearance services or procedures in the Cayman Islands, Hong Kong, the BVI, or any other relevant jurisdiction; or
 - (iv) a change or development occurs involving a change in taxation or exchange control (or the implementation of any exchange control) or currency exchange rates in the Cayman Islands, the PRC, Hong Kong, the BVI, or any other relevant jurisdiction; or
 - (v) any change or development involving a prospective change in the condition, financial or otherwise, or in the earnings, business affairs, business prospects or trading position of the Company or any member of the Group, including any litigation or claim of any third party being threatened or instigated against the Company or any member of the Group; or
 - (vi) any change or development involving a prospective change, or a materialisation of, any of the risks set out in the section headed “Risk Factors” in this prospectus; or

UNDERWRITING

- (vii) any general moratorium on commercial banking activities in Hong Kong (imposed by the Financial Secretary and/or the Hong Kong Monetary Authority or other competent authority), the Cayman Islands, the BVI, the PRC or any other relevant jurisdiction; or
- (viii) any outbreak or escalation of hostilities (whether or not war is or has been declared) or other state of emergency or calamity or wide-spread epidemic or political or social crisis involving the PRC, Hong Kong, the Cayman Islands, the BVI or any escalation thereof, or the declaration by the PRC, Hong Kong, the BVI or the Cayman Islands, of a national emergency or war; or
- (ix) any event of force majeure, including without limitation any act of God, war, riot, public disorder, civil commotion, economic sanctions, fire, flood, explosion, epidemic, terrorism (whether or not responsibility has been claimed), labour dispute, strike or lock-out involving the PRC, Hong Kong, the BVI, the Cayman Islands, or any other relevant jurisdiction; or
- (c) there comes to the notice of the Lead Manager any matter or event showing any of the warranties given by the Company and Controlling Shareholders (who are also the warrantors in the Underwriting Agreement) to be untrue, inaccurate or misleading in any respect which is or, in the sole and reasonable opinion of Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter), is likely to be material in the context of the Placing when given or repeated; or
- (d) there comes to the notice of the Lead Manager any breach on the part of the Company of any of the provisions of the Underwriting Agreement; or
- (e) any matter has arisen or been discovered which would, had it arisen or been discovered immediately before the date of this prospectus, not having been disclosed in this prospectus, constitutes a material omission therefrom; or
- (f) any statement contained in this prospectus, the Placing Shares, the formal notice of the Company and any announcements in the agreed form issued by the Company in connection with the Placing (including any amendment or supplement thereto) was, has or may become untrue, incorrect or misleading in any material respect; or
- (g) there shall have occurred any event, act or omission which gives or is likely to give rise to any liability of a material nature of the Group pursuant to the indemnities referred to in the Underwriting Agreement; or

UNDERWRITING

- (h) a valid demand by any creditor for repayment or payment of any indebtedness of the Company or any member of the Group or in respect of which the Company or any member of the Group is liable prior to its stated maturity is made, which demand has or could reasonably be expected to have a material adverse effect on the Group taken as a whole; or
- (i) a petition is presented for the winding-up or liquidation of the Company or any member of the Group, or the Company or any member of the Group makes any composition or arrangement with its creditors or enters into a scheme of arrangement or any resolution is passed for the winding-up, of the Company or any member of the Group or a provisional liquidator, receiver or manager is appointed over all or part of the assets or undertaking of the Company or any member of the Group or anything analogous thereto occurs in respect of the Company or any member of the Group,

which in the sole and reasonable opinion of Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) (1) is or will have or could be expected to have material adverse effect on the business, financial or other condition or prospects of the Group as a whole; or (2) has or will have or could reasonably be expected to have material adverse effect on the success, marketability or pricing of the Placing or the level of applications under the Placing; or (3) makes it inadvisable, inexpedient or impracticable for the Placing to proceed.

Commissions, fees and expenses

The Underwriter is expected to receive a commission of 3.5% of the aggregate Placing Price of all the Placing Shares. The Sponsor will, in addition, receive an advisory and documentation fee to the Placing. Based on the Placing Price of HK\$1.20 per Share (being the mid-point of the stated range of the Placing Price), the fees and commission, together with the Stock Exchange listing fees, the Stock Exchange trading fee and SFC transaction levy, legal and other professional fees, printing and other expenses relating to the Placing, are currently estimated to be approximately HK\$12.3 million in aggregate will be borne by the Company.

Underwriter's interest in the Company

Save as disclosed in this prospectus and as contemplated pursuant to the Underwriting Agreement, the Underwriter does not have any shareholding in any member of the Company or any right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Company.

UNDERWRITING

Pursuant to Rule 6A.19 of the GEM Listing Rules, we have appointed Shenyin Wanguo as our compliance adviser for the period commencing on the Listing Date and ending on the date on which our financial results for the second full financial year commencing after the Listing Date is required to be published in compliance with Rule 18.03 of the GEM Listing Rules.

UNDERTAKINGS

Each of the Controlling Shareholders has undertaken to and covenanted with the Company, Shenyin Wanguo (in the respective capacity as the Sponsor, the Lead Manager and the Underwriter) and the Stock Exchange for a period commencing on the date by reference to which disclosure of his/her/its shareholding in the Company is made in this prospectus and ending on the date which is 12 months following the Listing Date that:

- (a) in the first 6-month period, he/she/it shall not and shall procure that the relevant registered holders shall not dispose of, nor enter into any agreement to dispose of or otherwise create any options, rights, interests or encumbrances in respect of, any of the Shares in respect of which he/she/it is shown by this prospectus to be the beneficial owner (whether direct or indirect) (the “Relevant Shares”);
- (b) in the period of 6 months commencing on the date immediately following the date on which the first 6-month period referred to in paragraph (a) above expires, he/she/it shall not and shall procure that the relevant registered holders shall not dispose of, nor enter into any agreement to dispose of or otherwise create any options, rights, interests or encumbrances in respect of, any of the Relevant Shares if, immediately following such disposal or upon the exercise or enforcement of such options, rights, interests or encumbrances, he/she/it would cease to be a Controlling Shareholder;
- (c) in the event that he/she/it pledges or charges any of his/her/its direct or indirect interest in the Relevant Shares under Rule 13.18(1) of the GEM Listing Rules or pursuant to any right or waiver granted by the Stock Exchange pursuant to Rule 13.18(4) of the GEM Listing Rules at any time during the relevant periods specified in paragraphs (a) and (b) above, he/she/it must inform the Company, Shenyin Wanguo and the Stock Exchange immediately thereafter, disclosing the details as specified in Rule 17.43(1) to (4) of the GEM Listing Rules; and
- (d) having pledged or charged any of his/her/its interests in the Shares under paragraph (c) above, he/she/it must inform the Company, Shenyin Wanguo and the Stock Exchange immediately in the event that he/she/it becomes aware that the pledgee or chargee has disposed of or intends to dispose of such interest and of the number of the Relevant Shares so affected.

UNDERWRITING

The Company and each of the Controlling Shareholders and the executive Directors have undertaken to and covenanted with Shenyin Wanguo (in the respective capacity as the Sponsor, the Lead Manager and the Underwriter) to procure that, save with the prior written consent of Shenyin Wanguo (in both capacities as the Lead Manager and the Underwriter) or save as pursuant to the Placing, the Capitalisation Issue, or the grant of any option under the Pre-IPO Share Option Scheme or the Share Option Scheme, the Company will not, within six months from the Listing Date (a) save as permitted under the GEM Listing Rules (including but not limited to Rule 17.29 of the GEM Listing Rules) and the applicable laws, offer, allot or issue or agree to allot or issue any Shares or any other securities of the Company or grant or agree to grant any options, warrants or other rights carrying the rights to subscribe for, or otherwise convert into, or exchange for, any Shares or any other securities of the Company, and (b) purchase any Shares or any other securities of the Company.

The following is the full text of a report, prepared for the purpose of incorporation in this document, received from the auditors and reporting accountants of the Company, Deloitte Touche Tohmatsu, Certified Public Accountants, Hong Kong.

Deloitte.

德勤

德勤·關黃陳方會計師行
香港金鐘道88號
太古廣場一座35樓

Deloitte Touche Tohmatsu
35/F, One Pacific Place
88 Queenway
Hong Kong

28 October 2011

The Directors

RENHENG Enterprise Holdings Limited
Shenyin Wanguo Capital (H.K.) Limited

Dear Sirs/Madam,

We set out below our report on the financial information (the “Financial Information”) relating to RENHENG Enterprise Holdings Limited (the “Company”) and its subsidiaries (hereinafter collectively referred to as the “Group”) for each of the two years ended 31 December 2010 and for the six months ended 30 June 2011 (the “Relevant Periods”), for the inclusion in the prospectus of the Company dated 28 October 2011 (the “Prospectus”).

The Company was incorporated and registered as an exempted company in the Cayman Islands under the Companies Law of the Cayman Islands on 2 February 2011. Through a group reorganisation as more fully explained in the paragraph headed “Corporate Reorganisation” in Appendix V to the Prospectus (the “Group Reorganisation”), the Company has since 2 February 2011 become the holding company of the Group.

During the Relevant Periods and at the date of this report, the Company has the following subsidiaries:

Name of subsidiary	Place and date of incorporation/ establishment	Issued and fully paid share capital/ registered capital	Attributable equity interest to the Group			Principal activities
			31 December 2009	30 June 2010	At the date of report	
RENHENG Global Limited (formerly known as Yanlord Global Limited) (“Renheng Global”)	British Virgin Islands 15 October 2009	US\$50,000	100%	100%	100%	Investment holding
RENHENG Tech Limited (formerly known as Yanlord Tech Limited) (“Renheng Tech”)	Hong Kong 28 October 2009	HK\$1	100%	100%	100%	Investment holding
Bao Ying Ren Heng Industrial Co., Limited* (“Baoying Renheng”) (寶應仁恒實業有限公司) (wholly foreign-owned Enterprise)	People’s Republic of China (the “PRC”) 1 November 2001	RMB42,857,143	100%	100%	100%	Manufacture and sale of tobacco machinery products

* The English name is translated for identification purpose only.

Note: Renheng Global is directly held by the Company. Other subsidiaries are indirectly held by the Company.

All companies adopt 31 December as the financial year end date. The PRC statutory financial statements of the following subsidiary for each of the two years ended 31 December 2010 were prepared in accordance with the relevant accounting principles and financial regulations applicable to PRC enterprises (the "PRC GAAP") and were audited by the following certified public accountants registered in the PRC.

Name of subsidiary	Financial period	PRC auditor
Baoying Renheng	Year ended 31 December 2009	楊州潤楊恆信會計師事務所有限公司 Yangzhou Yunyang Hengxin CPA Co., Ltd.
	Year ended 31 December 2010	楊州潤楊恆信會計師事務所有限公司 Yangzhou Yunyang Hengxin CPA Co., Ltd.

We have acted as the auditor of Renheng Tech since its date of incorporation. The financial statements of Renheng Tech for the period from 28 October 2009 (date of incorporation) to 31 December 2010 were prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA"), except that the consolidated financial statements of Renheng Tech and its subsidiary have not been prepared in accordance with Hong Kong Accounting Standard 27 "Consolidated and Separate Financial Statements".

No audited financial statements have been prepared for Renheng Global which was incorporated in the British Virgin Islands where it is no statutory audit requirements.

No audited financial statements have been prepared for the Company for the period from the date of its incorporation as there is no statutory audit requirements in the Cayman Islands and the Company has not carried any business since its date of incorporation other than the transactions related to the Group Reorganisation.

For the purpose of this report, the directors of the Company have prepared the consolidated financial statements of the Group in accordance with HKFRSs issued by the HKICPA for each of the two years ended 31 December 2010 and for the six months ended 30 June 2011 (the "Underlying Financial Statements"). We have audited the Underlying Financial Statements in accordance with Hong Kong Standards on Auditing issued by the HKICPA and have examined the Underlying Financial Statements in accordance with the Auditing Guide 3.340 "Prospectuses and Reporting Accountant" as recommended by the HKICPA.

The Financial Information for the Relevant Periods set out in this report has been prepared from the Underlying Financial Statements on the basis set out in note 1 to the Financial Information. No adjustment was deemed necessary by us to the Underlying Financial Statements in preparing our report for inclusion in the Prospectus.

The Underlying Financial Statements are the responsibility of the directors of the Company who approve the issue. The directors of the Company are also responsible for the contents of the Prospectus in which this report is included. It is our responsibility to compile the Financial Information set out in this report from the Underlying Financial Statements, to form an independent opinion on the Financial Information and to report our opinion to you.

In our opinion, on the basis of presentation set out in note 1 to the Financial Information, the Financial Information together with the notes thereon gives, for the purpose of this report, a true and fair view of the state of affairs of the Group as at 31 December 2009, 31 December 2010 and 30 June 2011 and the Company as at 30 June 2011, and the consolidated profits and cash flows of the Group for the Relevant Periods.

The comparative consolidated statements of comprehensive income, changes in equity and cash flows of the Group for the six months ended 30 June 2010 together with the notes thereon have been extracted from the Group's unaudited financial information for the same period (the "30 June 2010 Financial Information") which was prepared by the directors of the Company solely for the purpose of this report. We have reviewed the 30 June 2010 Financial Information in accordance with the Hong Kong Standard of Review Engagements 2410 "Review of interim financial information performed by the independent auditor of the entity" issued by the HKICPA. Our review of the 30 June 2010 Financial Information consisted of making enquires, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion on the 30 June 2010 Financial Information. Based on our review, nothing has come to our attention that causes us to believe that the 30 June 2010 Financial Information is not prepared, in all material respects, in accordance with the accounting policies consistent with those used in the preparation of the Financial Information which conform with HKFRSs.

A. FINANCIAL INFORMATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Notes	Year ended 31 December		Six months ended 30 June	
		2009 HK\$'000	2010 HK\$'000	2010 HK\$'000 (unaudited)	2011 HK\$'000
Turnover	7	72,616	91,713	25,538	64,651
Cost of sales		<u>(44,195)</u>	<u>(51,099)</u>	<u>(15,800)</u>	<u>(43,776)</u>
Gross profit		28,421	40,614	9,738	20,875
Other income	8	3,877	4,279	2,154	1,038
Other gains and losses	9	34	713	510	(14)
Selling and distribution costs		(9,064)	(8,817)	(4,189)	(6,985)
Administrative expenses		(6,182)	(7,456)	(3,267)	(5,963)
Listing expenses		-	(1,595)	-	(2,225)
Interest on bank loans wholly repayable within five years		<u>(353)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Profit before taxation	10	16,733	27,738	4,946	6,726
Taxation	12	<u>(5,748)</u>	<u>(7,805)</u>	<u>(1,512)</u>	<u>(3,108)</u>
Profit for the year/period		10,985	19,933	3,434	3,618
Other comprehensive income:					
Exchange differences arising on translation		<u>592</u>	<u>2,775</u>	<u>622</u>	<u>2,235</u>
Total comprehensive income for the year/period		<u>11,577</u>	<u>22,708</u>	<u>4,056</u>	<u>5,853</u>
Earnings per share – basic	13	<u>7.3 HK cents</u>	<u>13.3 HK cents</u>	<u>2.3 HK cents</u>	<u>2.4 HK cents</u>

STATEMENTS OF FINANCIAL POSITION

	Notes	The Group		The Company	
		At 31 December 2009	At 31 December 2010	At 30 June 2011	At 30 June 2011
		HK\$'000	HK\$'000	HK\$'000	HK\$'000
Non-current assets					
Property, plant and equipment	14	14,261	14,664	15,197	–
Land use rights	15	2,972	3,002	3,035	–
Investment properties	16	16,930	18,305	18,999	–
Investment in a subsidiary	17	–	–	–	378
		<u>34,163</u>	<u>35,971</u>	<u>37,231</u>	<u>378</u>
Current assets					
Inventories	18	21,851	17,928	22,112	–
Trade and other receivables	19	21,440	42,503	46,511	78
Land use rights	15	68	71	72	–
Amounts due from customers for contract work	20	3,908	1,614	23,947	–
Amount due from ultimate holding company	21	388	–	–	–
Amounts due from related companies	22	7,056	417	427	–
Restricted bank deposit	23	–	237	243	–
Bank balances and cash	23	5,629	54,383	40,012	–
		<u>60,340</u>	<u>117,153</u>	<u>133,324</u>	<u>78</u>
Current liabilities					
Trade and other payables	24	18,029	41,450	68,155	38
Amount due to a customer for contract work	20	–	8,061	–	–
Amounts due to related companies	25	519	2,500	–	–
Amount due to a subsidiary	26	–	–	–	78
Tax payable		3,788	5,959	1,957	–
		<u>22,336</u>	<u>57,970</u>	<u>70,112</u>	<u>116</u>
Net current assets (liabilities)		<u>38,004</u>	<u>59,183</u>	<u>63,212</u>	<u>(38)</u>
Total assets less current liabilities		72,167	95,154	100,443	340
Non-current liabilities					
Deferred tax liabilities	27	794	1,073	509	–
		<u>71,373</u>	<u>94,081</u>	<u>99,934</u>	<u>340</u>
Capital and reserves					
Share capital	28	390	390	–	–
Reserves		70,983	93,691	99,934	340
Total equity		<u>71,373</u>	<u>94,081</u>	<u>99,934</u>	<u>340</u>

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

	Paid-in capital/ share capital HK\$'000	Merger reserve HK\$'000 (Note a)	Discretionary surplus reserve HK\$'000 (Note b)	Statutory surplus reserve HK\$'000 (Note b)	Capital reserve HK\$'000	Property revaluation reserve HK\$'000	Translation reserve HK\$'000	Accumulated (losses) profits HK\$'000	Total HK\$'000
At 1 January 2009	48,701	-	3,338	4,851	-	2,775	754	(2,012)	58,407
Profit for the year	-	-	-	-	-	-	-	10,985	10,985
Exchange differences arising on translation	-	-	-	-	-	-	592	-	592
Total comprehensive income for the year	-	-	-	-	-	-	592	10,985	11,577
Issue of shares	390	-	-	-	-	-	-	-	390
Capital contribution from a shareholder	-	-	-	-	999	-	-	-	999
Transfer	-	-	-	26	-	-	-	(26)	-
Transfer upon the group reorganisation	(48,701)	48,701	-	-	-	-	-	-	-
At 31 December 2009	390	48,701	3,338	4,877	999	2,775	1,346	8,947	71,373
Profit for the year	-	-	-	-	-	-	-	19,933	19,933
Exchange differences arising on translation	-	-	-	-	-	-	2,775	-	2,775
Total comprehensive income for the year	-	-	-	-	-	-	2,775	19,933	22,708
At 31 December 2010	390	48,701	3,338	4,877	999	2,775	4,121	28,880	94,081
Profit for the period	-	-	-	-	-	-	-	3,618	3,618
Exchange differences arising on translation	-	-	-	-	-	-	2,235	-	2,235
Total comprehensive income for the period	-	-	-	-	-	-	2,235	3,618	5,853
Transfer	-	-	-	1,176	-	-	-	(1,176)	-
Issue of shares arising from the group reorganisation	(390)	390	-	-	-	-	-	-	-
At 30 June 2011	<u>390</u>	<u>49,091</u>	<u>3,338</u>	<u>6,053</u>	<u>999</u>	<u>2,775</u>	<u>6,356</u>	<u>31,322</u>	<u>99,934</u>
At 1 January 2010	390	48,701	3,338	4,877	999	2,775	1,346	8,947	71,373
Profit for the period	-	-	-	-	-	-	-	3,434	3,434
Exchange differences arising on translation	-	-	-	-	-	-	622	-	622
Total comprehensive income for the period	-	-	-	-	-	-	622	3,434	4,056
At 30 June 2010 (unaudited)	<u>390</u>	<u>48,701</u>	<u>3,338</u>	<u>4,877</u>	<u>999</u>	<u>2,775</u>	<u>1,968</u>	<u>12,381</u>	<u>75,429</u>

Notes:

- (a) The merger reserve of the Group represented paid-in capital of Baoying Renheng and Renheng Global transferred from paid-in capital pursuant to the Group Reorganisation.

- (b) As stipulated by the relevant laws and regulations in the PRC, Baoying Renheng is required to maintain two reserves, being a statutory surplus reserve and a discretionary surplus reserve which are non-distributable. Appropriations to such reserves are made out of profit after taxation of Baoying Renheng determined based on PRC GAAP while the amount and allocation basis are decided by its board of directors annually. Pursuant to the relevant laws and regulations in the PRC, appropriation to the statutory surplus reserve is required until the balance reaches 50% of the registered capital. The statutory surplus reserve and the discretionary surplus reserve can be used to make up its prior year losses, if any, and can be applied in conversion into capital by means of capitalisation issue.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended		Six months ended	
	31 December 2009 HK\$'000	2010 HK\$'000	30 June 2010 HK\$'000 (unaudited)	2011 HK\$'000
Operating activities				
Profit before taxation	16,733	27,738	4,946	6,726
Adjustments for:				
Depreciation of property, plant and equipment	1,080	1,086	526	655
Loss on disposal of property, plant and equipment	–	73	5	–
Interest expense	353	–	–	–
Allowance for inventories	847	341	–	–
Allowance for doubtful debts	–	–	–	288
Operating lease rentals in respect of land use rights	68	69	34	36
Interest income	(85)	(210)	(62)	(157)
Gain on fair value changes of investment properties	(34)	(786)	(515)	(274)
Imputed interest income on retention money receivables	(133)	(44)	(22)	–
Operating cash flows before movements in working capital	18,829	28,267	4,912	7,274
(Increase) decrease in inventories	(5,956)	4,523	(7,575)	(3,844)
Increase in trade and other receivables	(473)	(19,550)	(2,132)	(3,038)
(Increase) decrease in amounts due from customers for contract work	(3,908)	2,426	3,937	(22,302)
(Increase) decrease in amounts due from related companies	(236)	4,504	(222)	(10)
Increase in trade and other payables	5,127	22,773	13,610	25,919
Increase (decrease) in amount due to a customer for contract work	–	8,061	4,637	(8,214)
Cash generated from (used in) operations	13,383	51,004	17,167	(4,215)
PRC Enterprise Income Tax paid	(4,260)	(5,550)	(2,911)	(7,790)
Net cash from (used in) operating activities	9,123	45,454	14,256	(12,005)
Investing activities				
Repayment from related companies	1,644	3,185	–	–
Interest received	85	210	62	157
Advance to related companies	(2,404)	(809)	–	–
(Advance to) repayment from ultimate holding company	(388)	388	–	–
Purchase of property, plant and equipment	(258)	(1,103)	(62)	(851)
Proceeds from disposal of property, plant and equipment	–	23	23	–
Addition in restricted bank deposit	–	(237)	–	–
Net cash (used in) from investing activities	(1,321)	1,657	23	(694)
Financing activities				
Advance from related companies	21	2,500	343	650
Issue of shares	390	–	–	–
Repayments of bank loans	(11,342)	–	–	–
Interests paid	(353)	–	–	–
Capital contribution from a shareholder	999	–	–	–
Prepayment for share issue costs	–	(532)	–	(605)
Repayment to related companies	–	(539)	–	(3,150)
Net cash (used in) from financing activities	(10,285)	1,429	343	(3,105)
Net (decrease) increase in cash and cash equivalents	(2,483)	48,540	14,622	(15,804)
Cash and cash equivalents at beginning of the year/period	8,017	5,629	5,629	54,383
Effect of foreign exchange rate changes	95	214	46	1,433
Cash and cash equivalents at end of the year/period, represented by bank balances and cash	5,629	54,383	20,297	40,012

NOTES TO THE FINANCIAL INFORMATION

1. GROUP REORGANISATION AND BASIS OF PRESENTATION OF FINANCIAL INFORMATION

In preparation of the listing of the Company's shares on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited ("GEM"), the Company underwent the Group Reorganisation which includes the following steps:

- (a) During the Relevant Periods, the business of the Group was carried out by Baoying Renheng which was under control by Mr. Wei Sheng Peng jointly with his spouse Ms. Liu Li (the "Controlling Shareholders"). On 15 October 2009, Renheng Global was incorporated in the British Virgin Islands and owned by Yanlord Industry Investment Limited ("Yanlord Industry Investment"), a company beneficially owned by the Controlling Shareholders.
- (b) On 28 October 2009, Renheng Tech, a wholly owned subsidiary of Renheng Global, was incorporated and acquired the entire beneficial interests in Baoying Renheng from Yanlord Industry Investment at nil consideration.
- (c) On 15 December 2010, LinkBest Capital Group Limited ("LinkBest") and Open Venture Global Limited ("Open Venture"), companies wholly owned by Mr. Wei Sheng Peng and Ms. Liu Li, respectively, acquired the entire beneficial interests in Renheng Global from Yanlord Industry Investment.
- (d) On 2 February 2011, the Company was incorporated by LinkBest and Open Venture, and registered as an exempted company in the Cayman Islands. Pursuant to a share swap agreement dated 2 February 2011, the Company acquired the entire equity interests in Renheng Global by issuing and allotting a total of 100 shares of HK\$0.01 each to LinkBest and Open Venture. Thereafter, the Company has become the holding company of the Group since 2 February 2011.

The Group resulting from the Group Reorganisation is regarded as a continuing entity. Accordingly, the consolidated statements of comprehensive income and cash flows for the Relevant Periods include the results and cash flows of the companies now comprising the Group, as if the group structure upon the completion of the Group Reorganisation had been in existence throughout the Relevant Periods, or since their respective dates of incorporation where this is a shorter period. The consolidated statements of financial position as at 31 December 2009 and 31 December 2010 have been prepared to present the assets and liabilities of the entities now comprising the Group as at the respective dates.

The functional currency of the Company is Renminbi as it is the currency in which the majority of the Group's transactions are denominated. The Financial Information of the Group is presented in Hong Kong dollars ("HK\$") as the management considers this presentation to be more useful for its current and potential investors.

2. APPLICATION OF HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs")

The HKICPA has issued a number of new and revised Hong Kong Accounting Standards ("HKASs"), HKFRSs, amendments and interpretations which are effective for the Group's accounting periods beginning on 1 January 2011. For the purpose of preparing and presenting the Financial Information of the Relevant Periods, the Group has adopted all these new and revised Standards and Interpretations consistently throughout the Relevant Periods.

The Group has not early applied the following new and revised standards and amendments that have been issued but are not yet effective:

HKFRS 1 (Amendments)	Severe hyperinflation and removal of fixed dates for first-time adopters ¹
HKFRS 7 (Amendments)	Disclosures – Transfers of financial assets ¹
HKFRS 9	Financial instruments ²
HKFRS 10	Consolidated financial statements ²
HKFRS 11	Joint arrangements ²
HKFRS 12	Disclosure of interests in other entities ²
HKFRS 13	Fair value measurement ²
HKAS 1 (Amendments)	Presentation of items of other comprehensive income ⁴
HKAS 12 (Amendments)	Deferred tax: Recovery of underlying assets ³
HKAS 19 (Revised 2011)	Employee benefits ²
HKAS 27 (Revised 2011)	Separate financial statements ²
HKAS 28 (Revised 2011)	Investments in associates and joint ventures ²

- ¹ Effective for annual periods beginning on or after 1 July 2011.
- ² Effective for annual periods beginning on or after 1 January 2013.
- ³ Effective for annual periods beginning on or after 1 January 2012.
- ⁴ Effective for annual periods beginning on or after 1 July 2012.

The management anticipates that the application of these new and revised standards, amendments and interpretations will have no material impact on the results and the financial position of the Group.

3. SIGNIFICANT ACCOUNTING POLICIES

The Financial Information has been prepared under the historical cost basis, except for investment properties which are measured at fair values, and in accordance with the following accounting policies which conform with HKFRSs. In addition, the Financial Information includes applicable disclosures required by the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited and by the Hong Kong Companies Ordinance.

Basis of consolidation

The Financial Information incorporates the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Investment in a subsidiary

Investment in a subsidiary is included in the statement of financial position of the Company at cost less any identified impairment loss.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold and services provided in the normal course of business, net of discounts and sales related taxes.

Revenue from sales of goods is recognised when goods are delivered and title has passed.

Revenue from construction contracts is recognised using the percentage of completion method by reference to the value of work carried out during the year/period as determined by progress verification certificate.

Rental income, including rental invoiced in advance from investment properties let under operating leases, is recognised on a straight line basis over the relevant lease terms.

Interest income from a financial asset is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount on initial recognition.

Property, plant and equipment

Property, plant and equipment including buildings held for use in production or supply of goods or services, or for administrative purposes are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of items of property, plant and equipment over their estimated useful lives and after taking into account of their estimated residual value, using the straight line method.

If an item of property, plant and equipment becomes an investment property because its use has changed as evidenced by end of owner-occupation, any difference between the carrying amount and the fair value of that item at the date of transfer is recognised in other comprehensive income and accumulated in property revaluation reserve. On the subsequent sale or retirement of the asset, the relevant revaluation reserve will be transferred directly to accumulated profits.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in profit or loss in the period in which the item is derecognised.

Investment properties

Investment properties are properties held to earn rentals and/or capital appreciation.

On initial recognition, investment properties are measured at cost, including any directly attributable expenditure. Subsequent to initial recognition, investment properties are measured at their fair values using the fair value model based on the valuation carried out by an independent property valuer. Gains or losses arising from changes in the fair value of investment property are included in profit or loss for the period in which they arise.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposals. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the profit or loss in the period in which the item is derecognised.

Construction contracts

Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the end of the reporting period, as measured by progress verification certificate. Variations in contract work, claims and incentive payments are included to the extent that the amount can be measured reliably and its receipt is considered probable.

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred that it is probable will be recoverable. Contract costs are recognised as expenses in the period in which they are incurred.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is shown as amounts due from customers for contract work. For contracts where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is shown as amounts due to customers for contract work. Amounts received before the related work is performed are included in the consolidated statement of financial position, as a liability, as advances from customers. Amounts billed for work performed but not yet paid by the customer are included in the consolidated statement of financial position under trade and other receivables.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessee

Operating lease payments are recognised as an expense on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a liability and release as a reduction of rental expense over the lease term on a straight-line basis.

The Group as lessor

Rental income from operating leases is recognised in profit or loss on a straight line basis over the relevant lease term.

Land use rights

When a lease includes both land and building elements, the Group assesses the classification of each element as a finance or an operating lease separately based on the assessment as to whether substantially all the risks and rewards incidental to ownership of each element have been transferred to the Group. Specifically, the minimum lease payments (including any lump-sum upfront payments) are allocated between the land and the building elements in proportion to the relative fair values of the leasehold interests in the land element and building element of the lease at the inception of the lease.

To the extent the allocation of the lease payments can be made reliably, interest in leasehold land that is accounted for as an operating lease is presented as "land use rights" in the consolidated statement of financial position and is released over the lease term on a straight line basis except for those that are classified and accounted for as investment properties under the fair value model. When the lease payments cannot be allocated reliably between the land and building elements, the entire lease is generally classified as a finance lease and accounted for as property, plant and equipment, unless it is clear that both elements are operating leases, in which case the entire lease is classified as an operating lease.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is calculated using the weighted average method.

Financial instruments

Financial assets and financial liabilities are recognised in the statement of financial position when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets or financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition.

Financial assets

The Group's and the Company's financial assets are mainly classified into loans and receivables.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

Interest income is recognised on an effective interest basis for debt instruments.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables (including trade and other receivables, amount due from ultimate holding company, amounts due from related companies, restricted bank deposit and bank balances and cash) are measured at amortised cost using the effective interest method, less any identified impairment losses (see accounting policy on impairment loss on financial assets below).

Impairment of financial assets

Financial assets are assessed for indicators of impairment at the end of the reporting periods. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been affected.

Objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation.

For certain categories of financial assets, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the credit period granted, observable changes in national or local economic conditions that correlate with default on receivables.

An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade and other receivables, where the carrying amount is reduced through the use of an allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss. When a receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited to profit or loss.

If, in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment loss was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Financial liabilities and equity instruments

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the group entity after deducting all of its liabilities.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

Interest expense is recognised on an effective interest basis for debt instruments.

Financial liabilities

Financial liabilities including trade and other payables, amounts due to related companies and amount due to a subsidiary are subsequently measured at amortised cost, using the effective interest method.

Equity instruments

Equity instruments issued by the group entity are recorded at the proceeds received, net of direct issue costs.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

Impairment

At the end of the reporting period, the Group reviews the carrying amounts of its assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year/period. Taxable profit differs from profit as reported in the consolidated statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable and deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the Financial Information and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences. Deferred tax assets are generally recognised to the extent that it is probable that taxable profit will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of the reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset is realised, based on tax rate (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities. Deferred tax is recognised in profit or loss, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case the deferred tax is also recognised in other comprehensive income or directly in equity respectively.

Foreign currencies

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At the end of the reporting period, monetary items denominated in foreign currencies are re-translated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not re-translated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are recognised in profit or loss in the period in which they arise.

For the purposes of presenting the Financial Information, the assets and liabilities of the group entity are translated from the functional currency of the respective companies into the presentation currency of the Group (i.e. HK\$) at the rate of exchange prevailing at the end of the reporting period, and their income and expenses are translated at the average exchange rates for the year/period, unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised in other comprehensive income and accumulated in equity (the translation reserve).

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sales, are added to the cost of those assets until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

Retirement benefit costs

Payments to state-managed retirement benefit schemes and the Mandatory Provident Fund ("MPF") Scheme, which are defined contribution schemes, are charged as expenses when employees have rendered service entitling them to the contributions.

Government grants

Government grants are not recognised until there is reasonable assurance that the Group will comply with the conditions attaching to them and that the grants will be received.

Government grants are recognised in profit or loss on a systematic basis over the periods in which the Group recognises as expenses the related costs for which the grants are intended to compensate. Government grants are recognised as revenue over the periods necessary to match them with the costs for which they are intended to compensate, on a systematic basis. Government grants that are receivable as compensation for expenses or losses already incurred or for the purpose of giving immediate financial support to the Group with no future related costs are recognised in profit or loss in the period in which they become receivable.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY

The key assumptions concerning the future, and other key sources of estimation uncertainty at the end of reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities, are described below.

Allowance for doubtful debts

The Group makes allowance for doubtful debts based on an assessment of the recoverability of trade and other receivables. Allowances are made on trade and other receivables whenever there is any objective evidence that the balances may not be collectible. The Group makes judgement in assessing the collectability based on observable data including creditworthiness and payment history of the customers (for details please refer to note 19). When objective evidence for allowance exists, the amount of allowance is the difference between the carrying amounts of the debts and the present value of estimated future cash flows, discounted at the effective interest rate. Where the expectation on the recoverability of the debts is different from the original estimate, such difference will impact the carrying amounts of trade and other receivables and doubtful debt expenses in the periods in which such estimate has been changed.

At 31 December 2009, 31 December 2010 and 30 June 2011, the carrying amounts of trade and other receivables, net of allowance, are HK\$17,673,000, HK\$29,167,000 and HK\$30,755,000, respectively.

Allowance for inventories

The Group makes allowance for inventories based on an assessment of the net realisable value of inventories. Allowances are applied to inventories where events or changes in circumstances indicate that the net realisable value is lower than the cost of inventories. The identification of obsolete inventories requires the use of judgement and estimates on the conditions and usefulness of the inventories. In cases where the net realisable value of inventories assessed are less than expected, a material recognition of allowance for inventories may arise, which would be recognised in profit or loss in the period in which such recognition takes place.

At 31 December 2009, 31 December 2010 and 30 June 2011, the carrying amounts of inventories are HK\$21,851,000, HK\$17,928,000 and HK\$22,112,000, respectively.

Construction contracts

Revenue from construction contract is recognised under the percentage of completion method which requires estimation made by the management. Anticipated losses are fully provided on contracts when identified. The management estimates the contract revenue, contract costs and foreseeable losses of construction based on the budgets prepared for the contracts. Because of the nature of the activities undertaken in construction businesses, the management reviews and revises the estimates of both contract revenue and contract costs in the budget prepared for each contract as the contract progresses. Where the actual contract revenue is less than expected or actual contract costs are more than expected, additional losses may need to be recognised.

5. CAPITAL RISK MANAGEMENT

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to stakeholders through the optimisation of the debt and equity balance. The overall strategy remains unchanged during the Relevant Periods.

The capital structure of the Group consists of equity attributable to owners of the Company, comprising paid-in capital/issued share capital and reserves.

The management reviews the capital structure on a regular basis. As part of this review, the management considers the cost of capital and the risks associated with each class of capital. Based on recommendations of the management, the Group will balance its overall capital structure through the payment of dividends and raising of new capital.

6. FINANCIAL INSTRUMENTS**(a) Categories of financial instruments****THE GROUP**

	At 31 December		At 30 June
	2009	2010	2011
	<i>HK\$'000</i>	<i>HK\$'000</i>	<i>HK\$'000</i>
Financial assets			
Loans and receivables (including cash and cash equivalents)	30,746	84,204	71,437
Financial liabilities			
Amortised cost	<u>13,304</u>	<u>25,665</u>	<u>50,101</u>

THE COMPANY

At 30 June
2011
HK\$'000

Financial liabilities

Amortised cost

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(b) Financial risk management objectives and policies

The Group's and the Company's financial instruments include trade and other receivables, amount due from ultimate holding company, amounts due from/to related companies, restricted bank deposit, bank balances and cash, trade and other payables and amount due to a subsidiary.

Details of these financial instruments are disclosed in respective notes. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. The management manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner. There has been no material change to the Group's exposure to market risks or the manner in which it manages and measures the risk over the Relevant Periods.

Interest rate risk

The Group's bank balances have exposure to cash flow interest rate risk due to the fluctuation of the prevailing market interest rate on restricted bank deposit and bank balances (see note 23 for details of these deposits) at the end of the reporting period. The management considers the Group's exposure of the short-term bank deposits and balances to interest rate risk is not significant as interest bearing bank deposits and balances are within short maturity period.

Credit risk

The Group's maximum exposure to credit risk in the event of the counterparties' failure to perform their obligations at the end of the reporting period in relation to each class of recognised financial asset is the carrying amount of those assets as stated in the consolidated statement of financial position. In order to manage the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews the recoverable amount of each individual debt at the end of the reporting period to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the management considers that the Group's credit risk is significantly reduced.

The credit risk on liquid funds is limited because the counterparties are banks with high credit-ratings assigned by international credit-rating agencies.

The Group has concentration of credit risk as 70%, 60% and 65% of the aggregate amount of trade receivables and retention money receivables was due from the Group's five largest customers, operated in the tobacco industry in the PRC, as at 31 December 2009, 31 December 2010 and 30 June 2011, respectively. In order to minimise the credit risk, management continuously monitors the level of exposure to ensure that follow-up actions and/or corrective actions are taken promptly to lower the risk exposure or to recover overdue balances.

Liquidity risk

In the management of the liquidity risk, the Group monitors and maintains a level of cash and cash equivalents deemed adequate by the management to finance the Group's operations and mitigate the effects of fluctuation in cash flows.

The following table details the Group's and the Company's remaining contractual maturity for its financial liabilities based on the agreed repayment terms. The table has been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group and the Company can be required to pay. The table represented principal cash flows since the balances are non-interest bearing.

Liquidity tables

	Weighted average effective interest rate	Repayable on demand <i>HK\$'000</i>	Less than 3 months <i>HK\$'000</i>	Total undiscounted cash flows <i>HK\$'000</i>	Total carrying amounts <i>HK\$'000</i>
THE GROUP					
At 31 December 2009					
Trade and other payables	–	3,051	9,734	12,785	12,785
Amounts due to related companies	–	519	–	519	519
		<u>3,570</u>	<u>9,734</u>	<u>13,304</u>	<u>13,304</u>
At 31 December 2010					
Trade and other payables	–	4,334	18,831	23,165	23,165
Amount due to a related company	–	2,500	–	2,500	2,500
		<u>6,834</u>	<u>18,831</u>	<u>25,665</u>	<u>25,665</u>
At 30 June 2011					
Trade and other payables	–	4,636	45,465	50,101	50,101
THE COMPANY					
At 30 June 2011					
Other payables	–	38	–	38	38
Amount due to a subsidiary	–	78	–	78	78
		<u>116</u>	<u>–</u>	<u>116</u>	<u>116</u>

(c) Fair value

The fair value of financial assets and financial liabilities is determined in accordance with generally accepted pricing models based on discounted cash flow analysis.

The management considers that the carrying amounts of financial assets and financial liabilities recorded at amortised cost in the Financial Information approximate to their fair values.

7. TURNOVER AND SEGMENT INFORMATION

Turnover represents revenue arising from sale of goods and construction contracts of casing and flavouring system for the Relevant Periods. An analysis of the Group's revenue for the Relevant Periods is as follows:

	Year ended		Six months ended	
	31 December		30 June	
	2009	2010	2010	2011
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Sales of goods	23,455	30,525	7,787	7,277
Revenue from construction contracts of casing and flavouring system	49,161	61,188	17,751	57,374
	<u>72,616</u>	<u>91,713</u>	<u>25,538</u>	<u>64,651</u>

The Group's operating activities are attributable to a single operating segment focusing on manufacture and sale of tobacco machinery products. This operating segment has been identified on the basis of internal management reports prepared in accordance with accounting policies conform to HKFRSs, that are regularly reviewed by the chief executive officer of the Group, the chief operating decision maker of the Group. The chief executive officer of the Group regularly reviews revenue analysis by products, including casing and flavouring system, pneumatic feeding system, pre-pressing packing system and other products. However, other than revenue analysis, no operating results and other discrete financial information is available for the assessment of performance of the respective products. The chief executive officer of the Group reviews the revenue and the profit for the year/period of the Group as a whole to make decision about resources allocation. No analysis of segment assets or segment liabilities is presented as they are not regularly provided to the chief executive officer of the Group. Accordingly, no analysis of this single operating segment is presented.

Entity-wide information

An analysis of the Group's turnover by products is as follows:

	Year ended		Six months ended	
	31 December		30 June	
	2009	2010	2010	2011
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Sales of				
– casing and flavouring system	49,161	61,188	17,751	57,374
– pneumatic feeding system	12,399	17,805	6,407	2,476
– pre-pressing packing system	5,663	8,476	510	273
– other products	5,393	4,244	870	4,528
	<u>72,616</u>	<u>91,713</u>	<u>25,538</u>	<u>64,651</u>

Revenue from customers of the corresponding years/periods contributing over 10% of the total sales of the Group are as follows:

	Year ended 31 December		Six months ended 30 June	
	2009 HK\$'000	2010 HK\$'000	2010 HK\$'000 (unaudited)	2011 HK\$'000
Customer A ¹	53,208	60,589	22,197	21,893
Customer B ²	<u>–</u>	<u>–</u>	<u>–</u>	<u>30,412</u>

¹ Revenue from sales of all products.

² Revenue from sales of casing and flavouring system. There is no revenue contributed over 10% of the total sales of the Group during the two years ended 31 December 2009 and 2010 and the six months ended 30 June 2010.

During the Relevant Periods, all of the Group's turnover are arisen in the PRC, which are determined by the location where the system or products being installed or delivered. The Group's non-current assets of HK\$34,163,000, HK\$35,971,000 and HK\$37,181,000 as at 31 December 2009, 31 December 2010 and 30 June 2011, respectively, are arisen in and located in the PRC. The Group's non-current assets of HK\$50,000 as at 30 June 2011 are arisen in and located in Hong Kong.

8. OTHER INCOME

	Year ended 31 December		Six months ended 30 June	
	2009 HK\$'000	2010 HK\$'000	2010 HK\$'000 (unaudited)	2011 HK\$'000
Sales of materials	2,114	1,975	540	446
Rental income	804	819	405	422
Interest income	85	210	62	157
Imputed interest income on retention money receivables	133	44	22	–
Subsidy income (<i>note</i>)	74	1,138	1,125	–
Others	<u>667</u>	<u>93</u>	<u>–</u>	<u>13</u>
	<u>3,877</u>	<u>4,279</u>	<u>2,154</u>	<u>1,038</u>

Note: Based on document issued by the People's Government of Baoying, Baoying Renheng is entitled to tax refund based on PRC enterprise income tax paid in prior year and approximately 12.5% of the excess of amount of value-added tax paid in prior year as compared with the reference amount as stated in the document.

9. OTHER GAINS AND LOSSES

	Year ended 31 December		Six months ended 30 June	
	2009 HK\$'000	2010 HK\$'000	2010 HK\$'000 (unaudited)	2011 HK\$'000
Gain on fair value changes of investment properties	34	786	515	274
Loss on disposal of property, plant and equipment	-	(73)	(5)	-
Allowance for doubtful debts	-	-	-	(288)
	<u>34</u>	<u>713</u>	<u>510</u>	<u>(14)</u>

10. PROFIT BEFORE TAXATION

	Year ended 31 December		Six months ended 30 June	
	2009 HK\$'000	2010 HK\$'000	2010 HK\$'000 (unaudited)	2011 HK\$'000
Profit before taxation has been arriving at after charging:				
Directors' remuneration (<i>note 11</i>)	-	-	-	-
Other staff costs	5,923	7,812	3,334	4,709
Retirement benefits scheme contributions	188	214	147	181
Total staff costs	6,111	8,026	3,481	4,890
Depreciation of property, plant and equipment	1,080	1,086	526	655
Allowance for inventories, included in costs of sales	847	341	-	-
Auditor's remuneration	610	285	125	263
Cost of inventories recognised as an expense	11,675	12,318	2,827	3,745
Operating lease rentals in respect of land use rights	68	69	34	36
Operating lease payments in respect of a rented premise	-	-	-	72
	<u>-</u>	<u>-</u>	<u>-</u>	<u>72</u>

11. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

No emoluments was paid or payable to the directors of the Company during the Relevant Periods. The emoluments of five highest paid individuals during the Relevant Periods were as follows:

	Year ended 31 December		Six months ended 30 June	
	2009 HK\$'000	2010 HK\$'000	2010 HK\$'000	2011 HK\$'000
			(unaudited)	
Employees				
– basic salaries, bonus and allowances	580	801	663	893
– retirement benefits scheme contributions	24	22	11	18
	<u>604</u>	<u>823</u>	<u>674</u>	<u>911</u>

The emoluments of each of the five highest paid individuals during the Relevant Periods were below HK\$1,000,000.

During the Relevant Periods, no emoluments were paid by the Group to the directors of the Company or the five highest paid individual as an inducement to join or upon joining the Group or as compensation for loss of office. No directors waived any emoluments during the Relevant Periods.

12. TAXATION

	Year ended 31 December		Six months ended 30 June	
	2009 HK\$'000	2010 HK\$'000	2010 HK\$'000	2011 HK\$'000
			(unaudited)	
The charge comprises:				
PRC Enterprise Income Tax – current year/period	5,224	7,557	1,315	3,041
Withholding tax on distributed profit	–	–	–	657
Deferred taxation (<i>note 27</i>)	524	248	197	(590)
	<u>5,748</u>	<u>7,805</u>	<u>1,512</u>	<u>3,108</u>

No provision for Hong Kong Profits Tax has been made in the Financial Information as the Group has no assessable profit arisen in, or was derived from, Hong Kong.

The provision for PRC Enterprise Income Tax is based on the estimated taxable income for PRC taxation purposes at 25% pursuant to the Law of the PRC on Enterprise Income Tax and Implementation Legislation.

The tax charge for the Relevant Periods can be reconciled to the profit before taxation per the consolidated statement of comprehensive income as follows:

	Year ended 31 December		Six months ended 30 June	
	2009 HK\$'000	2010 HK\$'000	2010 HK\$'000 (unaudited)	2011 HK\$'000
Profit before taxation	<u>16,733</u>	<u>27,738</u>	<u>4,946</u>	<u>6,726</u>
Tax at the applicable tax rate of 25%	4,183	6,935	1,237	1,682
Tax effect of expenses not deductible for tax purposes	963	716	275	1,189
Tax effect of income not taxable for tax purposes	(44)	(4)	–	(4)
Effect of different tax rates of subsidiaries in other jurisdictions	53	158	–	241
Withholding tax on undistributed profits	<u>593</u>	<u>–</u>	<u>–</u>	<u>–</u>
Tax charge for the year/period	<u>5,748</u>	<u>7,805</u>	<u>1,512</u>	<u>3,108</u>

13. EARNINGS PER SHARE

The calculation of the basic earnings per share for the Relevant Periods is based on the following data and on the assumption that the Group Reorganisation and the capitalisation issue of 149,999,900 shares as disclosed in “Statutory and General Information” in Appendix V to the Prospectus had been effective on 1 January 2009:

	Year ended 31 December		Six months ended 30 June	
	2009 HK\$'000	2010 HK\$'000	2010 HK\$'000 (unaudited)	2011 HK\$'000
Earnings				
Profit for the year/period attributable to owners of the Company for the purpose of basic earnings per share	<u>10,985</u>	<u>19,933</u>	<u>3,434</u>	<u>3,618</u>
Number of shares				
Number of ordinary shares for the purpose of basic earnings per share	<u>150,000,000</u>	<u>150,000,000</u>	<u>150,000,000</u>	<u>150,000,000</u>

No diluted earnings per share is presented as there was no potential ordinary share during the Relevant Periods.

14. PROPERTY, PLANT AND EQUIPMENT

	Buildings <i>HK\$'000</i>	Furniture, fixtures and office equipment <i>HK\$'000</i>	Computer equipment <i>HK\$'000</i>	Motor vehicles <i>HK\$'000</i>	Plant and machinery <i>HK\$'000</i>	Total <i>HK\$'000</i>
THE GROUP						
COST						
At 1 January 2009	15,167	393	734	1,430	4,507	22,231
Currency realignment	140	3	7	13	43	206
Additions	<u>–</u>	<u>3</u>	<u>29</u>	<u>–</u>	<u>226</u>	<u>258</u>
At 31 December 2009	15,307	399	770	1,443	4,776	22,695
Currency realignment	525	13	16	56	162	772
Additions	336	–	58	368	341	1,103
Disposals	<u>–</u>	<u>–</u>	<u>(635)</u>	<u>–</u>	<u>(300)</u>	<u>(935)</u>
At 31 December 2010	16,168	412	209	1,867	4,979	23,635
Currency realignment	369	10	5	51	114	549
Additions	<u>–</u>	<u>10</u>	<u>73</u>	<u>696</u>	<u>72</u>	<u>851</u>
At 30 June 2011	<u>16,537</u>	<u>432</u>	<u>287</u>	<u>2,614</u>	<u>5,165</u>	<u>25,035</u>
DEPRECIATION						
At 1 January 2009	2,413	243	565	771	3,291	7,283
Currency realignment	25	3	5	7	31	71
Provided for the year	<u>686</u>	<u>49</u>	<u>52</u>	<u>130</u>	<u>163</u>	<u>1,080</u>
At 31 December 2009	3,124	295	622	908	3,485	8,434
Currency realignment	119	10	11	33	117	290
Provided for the year	708	22	29	145	182	1,086
Eliminated on disposals	<u>–</u>	<u>–</u>	<u>(569)</u>	<u>–</u>	<u>(270)</u>	<u>(839)</u>
At 31 December 2010	3,951	327	93	1,086	3,514	8,971
Currency realignment	94	8	2	26	82	212
Provided for the period	<u>379</u>	<u>16</u>	<u>28</u>	<u>110</u>	<u>122</u>	<u>655</u>
At 30 June 2011	<u>4,424</u>	<u>351</u>	<u>123</u>	<u>1,222</u>	<u>3,718</u>	<u>9,838</u>
CARRYING VALUES						
At 31 December 2009	<u>12,183</u>	<u>104</u>	<u>148</u>	<u>535</u>	<u>1,291</u>	<u>14,261</u>
At 31 December 2010	<u>12,217</u>	<u>85</u>	<u>116</u>	<u>781</u>	<u>1,465</u>	<u>14,664</u>
At 30 June 2011	<u>12,113</u>	<u>81</u>	<u>164</u>	<u>1,392</u>	<u>1,447</u>	<u>15,197</u>

The above items of property, plant and equipment are depreciated at the following rate, after taking into account of their estimated residual values, on a straight line basis:

Buildings	5%
Furniture, fixtures and office equipment	20% – 33%
Computer equipment	33%
Motor vehicles	10% – 20%
Plant and machinery	20%

The Group's buildings are held under medium-term leases and are situated in the PRC.

15. LAND USE RIGHTS

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
THE GROUP			
CARRYING AMOUNT			
At beginning of the year/period	3,080	3,040	3,073
Currency realignment	28	102	70
Charge to profit or loss during the year/period	(68)	(69)	(36)
	<u>3,040</u>	<u>3,073</u>	<u>3,107</u>
At end of the year/period	<u>3,040</u>	<u>3,073</u>	<u>3,107</u>
Non-current asset	2,972	3,002	3,035
Current asset	68	71	72
	<u>3,040</u>	<u>3,073</u>	<u>3,107</u>

The Group's leasehold interest in land is held under medium-term leases and is situated in the PRC.

16. INVESTMENT PROPERTIES

	HK\$'000
THE GROUP	
FAIR VALUE	
At 1 January 2009	16,742
Currency realignment	154
Increase in fair value recognised in profit or loss	<u>34</u>
At 31 December 2009	16,930
Currency realignment	589
Increase in fair value recognised in profit or loss	<u>786</u>
At 31 December 2010	18,305
Currency realignment	420
Increase in fair value recognised in profit or loss	<u>274</u>
At 30 June 2011	<u>18,999</u>

The investment properties are measured using the fair value model at the end of the reporting period based on the valuation carried out by Greater China Appraisal Limited ("Greater China"), an independent property valuer, by adopting the direct comparison approach making reference to comparable sales evidence. The address of Greater China is Room 2703, Shui On Centre, 6-8 Harbour Road, Wanchai, Hong Kong.

The Group's investment properties are held under medium-term leases to earn rentals and are situated in the PRC.

17. INVESTMENT IN A SUBSIDIARY

At 30 June 2011

HK\$'000

THE COMPANY

Unlisted investment, at cost

378

18. INVENTORIES

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
THE GROUP			
Raw materials	7,797	7,379	10,334
Work in progress	14,054	10,549	11,778
	<u>21,851</u>	<u>17,928</u>	<u>22,112</u>

19. TRADE AND OTHER RECEIVABLES

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
THE GROUP			
Trade receivables	8,870	16,071	16,112
Less: Allowance for doubtful debts	(2,022)	(2,090)	(2,429)
	<u>6,848</u>	<u>13,981</u>	<u>13,683</u>
Retention money receivables – due within one year	6,080	11,272	12,452
Prepayments and deposits	3,767	10,192	13,634
Valued-added tax recoverable	–	3,144	2,122
Sundry receivables	5,199	4,384	5,100
Less: Allowance for doubtful debts	(454)	(470)	(480)
	<u>14,592</u>	<u>28,522</u>	<u>32,828</u>
	<u>21,440</u>	<u>42,503</u>	<u>46,511</u>

The Group normally allows a credit period of three months to its trade customers. Before accepting any new customer, the Group will internally assess the credit quality of the potential customer and define appropriate credit limits.

The following is an aged analysis of trade receivables (net of allowance for doubtful debts) presented based on the invoice date at the end of the reporting period.

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
0 – 90 days	3,177	9,265	6,525
91 – 365 days	3,326	4,149	6,126
1 – 2 years	147	279	1,032
Over 2 years	198	288	–
	<u>6,848</u>	<u>13,981</u>	<u>13,683</u>

The following is an aged analysis of trade receivables (net of allowance for doubtful debts) presented based on the invoice date at the end of the reporting period which are past due but not impaired as the management of the Group considers that there has not been a significant change in credit quality and the amounts are still considered recoverable. The Group does not hold any collateral over these balance.

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
91 – 365 days	3,326	4,149	6,126
1 – 2 years	147	279	1,032
Over 2 years	198	288	–
	<u>3,671</u>	<u>4,716</u>	<u>7,158</u>

The Group's management closely monitors the credit quality of receivables and considers those receivables that are neither past due nor impaired to be of a good credit quality.

Movement in the allowance for doubtful debts:

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
At beginning of the year/period	2,453	2,476	2,560
Currency realignment	23	84	61
Provided for the year/period	–	–	288
At end of the year/period	<u>2,476</u>	<u>2,560</u>	<u>2,909</u>

At 31 December 2009, 31 December 2010 and 30 June 2011, the allowance for doubtful debts represented individually impaired trade and other receivables which have been placed under liquidation or in severe financial difficulties. The Group does not hold any collateral over these balances.

At 30 June 2011
HK\$'000

THE COMPANY
Prepayments

78

20. AMOUNTS DUE FROM (TO) CUSTOMERS FOR CONTRACT WORK

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
THE GROUP			
Contracts in progress at the end of the reporting period			
Contract costs incurred plus recognised profits less recognised losses	8,704	24,191	72,737
Less: progress billings	(4,796)	(30,638)	(48,790)
	<u>3,908</u>	<u>(6,447)</u>	<u>23,947</u>
Analysed for reporting purposes as:			
Amounts due from customers for contract work	3,908	1,614	23,947
Amount due to a customer for contract work	—	(8,061)	—
	<u>3,908</u>	<u>(6,447)</u>	<u>23,947</u>

At 31 December 2009, 31 December 2010 and 30 June 2011, retentions held by the customers for contract works, included in Note 19, were amounted to HK\$3,991,000, HK\$8,588,000 and HK\$7,398,000, respectively, and advances received from customers for contract work, included in Note 24, were amounted to HK\$378,000, HK\$10,020,000 and HK\$5,849,000, respectively.

21. AMOUNT DUE FROM ULTIMATE HOLDING COMPANY

THE GROUP

The amount was unsecured, interest-free and repayable on demand.

22. AMOUNTS DUE FROM RELATED COMPANIES

THE GROUP

Details of the amounts due from related companies are as follows:

Name of related company	1.1.2009	31.12.2009	31.12.2010	30.6.2011	Maximum amount outstanding		
					Year ended 31 December 2009	Year ended 30 June 2010	Six months ended 30 June 2011
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
Yangzhou Jinchuang Curtain Wall Engineering Company Limited* (揚州金窗幕牆工程有限公司)	105	207	214	219	207	1,038	219
Yangzhou Longtai Electric Company Limited* (揚州龍泰電器有限公司)	5,898	6,849	203	208	6,849	7,285	365
	<u>6,003</u>	<u>7,056</u>	<u>417</u>	<u>427</u>			

* The English name is translated for identification purpose only.

Note: The Controlling Shareholders, being also the directors of the Company, have beneficial interests in these companies. Except for the amounts in trade nature of HK\$4,921,000, HK\$417,000 and HK\$427,000 as at 31 December 2009, 31 December 2010 and 30 June 2011, respectively, which are allowed for a credit period of three months, other amounts are unsecured, interest-free and repayable on demand.

The following is an aged analysis of trade balances with related companies for goods sold based on the invoice date at the end of the reporting period.

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
0 – 90 days	977	417	427
91 – 365 days	3,944	–	–
	4,921	417	427
	4,921	417	427

The balances with carrying amount of HK\$3,944,000, nil and nil are past due but not impaired at 31 December 2009, 31 December 2010 and 30 June 2011 respectively. The credit exposure of those balances is minimal as they were settled subsequently.

23. RESTRICTED BANK DEPOSIT/BANK BALANCES AND CASH

THE GROUP

Bank balances comprise short-term bank deposits carried at prevailing market deposit rate. As at 31 December 2009, 31 December 2010 and 30 June 2011, the effective interest rate of these deposits ranged from 0.36% to 1.15%, 0.36% to 1.50% and 0.50% to 1.50% per annum, respectively.

As at 31 December 2010 and 30 June 2011, restricted bank deposit represents a deposit of HK\$237,000 and HK\$243,000 with effective interest rate of 0.5% and 0.5% per annum pledged to a bank to secure default payment of certain percentage to contract sum upon default of the construction contract of a customer, respectively. The deposit will be released upon the completion of certificate from the customer.

24. TRADE AND OTHER PAYABLES

THE GROUP	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
Trade payables	11,634	21,999	49,046
Advances from customers	3,074	16,595	16,326
Accrued welfare expense	1,634	1,690	1,728
Valued-added tax payable	536	–	–
Other payables	1,151	1,166	1,055
	18,029	41,450	68,155
	18,029	41,450	68,155

The following is an aged analysis of trade payables presented based on the invoice date at the end of the reporting period.

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
0 – 90 days	9,734	18,831	44,411
91 – 365 days	1,629	1,833	3,442
1 – 2 years	11	1,064	913
2 – 3 years	260	271	280
	<u>11,634</u>	<u>21,999</u>	<u>49,046</u>

The average credit period on purchase of goods is 90 days.

At 30 June 2011
HK\$'000

THE COMPANY

Other payables 38

25. AMOUNTS DUE TO RELATED COMPANIES

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
Name of related company			
THE GROUP			
Zhuhai Mingtai Fine Chemical Company Limited* (珠海明泰精細化工有限公司)	500	–	–
Grand Bright International Enterprise Limited	19	2,500	–
	<u>519</u>	<u>2,500</u>	<u>–</u>

* *The English name is translated for identification purpose only.*

Note: The Controlling Shareholders, being also the directors of the Company, have beneficial interests in these companies. The amounts are non-trade nature, unsecured, interest-free and repayable on demand.

26. AMOUNT DUE TO A SUBSIDIARY

THE COMPANY

The amount is unsecured, interest-free and repayable on demand.

27. DEFERRED TAXATION

THE GROUP

The followings are the major deferred tax assets (liabilities) recognised and movements thereon during the Relevant Periods:

	Provision for trade and other receivables <i>HK\$'000</i>	Provision for inventories <i>HK\$'000</i>	Withholding tax on undistributed profits <i>HK\$'000</i>	Revaluation of investment properties <i>HK\$'000</i>	Total <i>HK\$'000</i>
At 1 January 2009	613	446	(26)	(1,299)	(266)
Currency realignment	6	4	(2)	(12)	(4)
Credit (charge) to profit or loss for the year	—	212	(593)	(143)	(524)
At 31 December 2009	619	662	(621)	(1,454)	(794)
Currency realignment	21	24	(21)	(55)	(31)
Credit (charge) to profit or loss for the year	—	85	—	(333)	(248)
At 31 December 2010	640	771	(642)	(1,842)	(1,073)
Currency realignment	15	18	(15)	(44)	(26)
Credit (charge) to profit or loss for the period	72	—	657	(139)	590
At 30 June 2011	<u>727</u>	<u>789</u>	<u>—</u>	<u>(2,025)</u>	<u>(509)</u>

The withholding tax on undistributed profits of a PRC subsidiary for the year ended 31 December 2009 has been fully recognised as deferred tax liability as at 31 December 2009 and 31 December 2010. During the six months ended 30 June 2011, the withholding tax on such distributed profits was settled and the balance of deferred tax liability has been released. As at 31 December 2010 and 30 June 2011, the Group does not recognise deferred tax liability in relation to withholding tax on undistributed profits of that PRC subsidiary of HK\$29,460,000 and HK\$43,976,000, respectively, because of the retention of undistributed profits by the subsidiary in the PRC was determined by the management.

28. PAID-IN CAPITAL/SHARE CAPITAL

	At 30 June 2011	
	Number of share	HK\$'000
THE COMPANY		
Authorised:		
Ordinary share of HK\$0.01 each	<u>38,750,000</u>	<u>388</u>
Issued and fully paid:		
Shares issue arising from the group reorganisation and balance at 30 June 2011	<u>100</u>	<u>—</u>

The Company was incorporated on 2 February 2011 with an authorised share capital of HK\$387,500 divided into 38,750,000 shares of HK\$0.01 each. Pursuant to a share swap agreement dated 2 February 2011, the Company acquired the entire issued share capital of Renheng Global from the Controlling Shareholders, and in consideration thereof, a total of 100 shares of the Company were issued and allotted to LinkBest and Open Venture, which are wholly owned by Mr. Wei Sheng Peng and Ms. Liu Li, respectively.

The paid-in capital of the Group as at 1 January 2009 represents the paid-in capital of Baoying Renheng.

The share capital of the Group as at 31 December 2009 and 31 December 2010 represents the share capital of Renheng Global.

29. LEASE COMMITMENTS

The Group as lessee

At the end of the reporting period, the Group was committed to make the following future minimum lease payments under an non-cancellable operating lease which fall due as follows:

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
Within one year	–	–	165
In the second to fifth years inclusive	–	–	90
	<u>–</u>	<u>–</u>	<u>255</u>

Lease is negotiated and rental is fixed originally for a lease term of two years.

The Group as lessor

At the end of the reporting period, the Group had contracted with related companies, companies controlled by Mr. Wei Sheng Peng and Ms. Liu Li, for the following future minimum lease payments:

	At 31 December		At 30 June
	2009	2010	2011
	HK\$'000	HK\$'000	HK\$'000
Within one year	807	834	853
In the second to fifth years inclusive	2,276	2,116	427
Over five years	1,242	854	–
	<u>4,325</u>	<u>3,804</u>	<u>1,280</u>

At 31 December 2009, 31 December 2010 and 30 June 2011, the investment properties have committed tenants for lease terms of 8 years, 7 years and 2 years, respectively. In January 2011, the Group and the related companies agreed to early terminate the tenancy agreements and entered into new tenancy agreements with shorter lease periods.

30. RETIREMENT BENEFITS SCHEME

The Group participates in the MPF Scheme registered with the Mandatory Provident Fund Scheme Authority under the Mandatory Provident Scheme Ordinance for all qualifying employees in Hong Kong. The assets of the scheme are held separately from those of the Group in funds under the control of trustee. The Group contributes 5% of relevant payroll costs with a cap of monthly contributions of HK\$1,000 to the MPF Scheme, which contribution is matched by employee.

The employees of the Group's PRC subsidiary are members of the state-managed retirement benefits scheme operated by the PRC government. The PRC subsidiary is required to contribute a certain percentage of its payroll cost to the retirement benefits scheme to fund the benefits. The only obligations of the Group with respect to the retirement benefits scheme is to make the required contributions under the scheme.

During the Relevant Periods, the amounts incurred for retirement benefit scheme contributions are disclosed in note 10. According to respective schemes, those contributions are not refundable or forfeitable.

31. RELATED PARTY TRANSACTIONS

Apart from details of the balances with related companies disclosed in the respective notes, the Group entered into the following transactions with related companies during the Relevant Periods:

Relationship of related parties	Nature of transactions	Year ended 31 December		Six months ended 30 June	
		2009 HK\$'000	2010 HK\$'000	2010 HK\$'000 (unaudited)	2011 HK\$'000
Continuing transactions					
Companies controlled by Mr. Wei Sheng Peng and Ms. Liu Li, beneficial shareholders of the Company	Rental income	804	819	405	422
Company controlled by Mr. Wei Sheng Peng and Ms. Liu Li, beneficial shareholders of the Company	Sales of goods	347	–	–	–
	Purchase of goods	34	434	–	11
	Subcontracting work	–	113	–	133
Transactions to be discontinued					
Company controlled by Mr. Wei Sheng Peng and Ms. Liu Li, beneficial shareholders of the Company	Purchase of property, plant and equipment	–	33	–	–

B. DIRECTORS' REMUNERATION

Save as disclosed herein, no remuneration has been paid or payable to the Company's directors by the Company or any of its subsidiaries during the Relevant Periods.

Under the arrangement currently in force, the aggregate amount of remuneration of the directors of the Company payable for the year ending 31 December 2011 is estimated to be approximately HK\$142,500.

C. SUBSEQUENT EVENT

Subsequent to 30 June 2011, written resolutions of shareholders of the Company were passed to approve the matters set out in the paragraph headed "Written resolutions of the Shareholders" passed on 20 October 2011 and set out in Appendix V to the Prospectus.

Save as aforesaid, no other significant events took place subsequent to 30 June 2011.

D. SUBSEQUENT FINANCIAL STATEMENTS

No audited financial statements have been prepared by the Company or any of the companies of the Group subsequent to 30 June 2011.

Yours faithfully,

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong

A. UNAUDITED PRO FORMA ADJUSTED NET TANGIBLE ASSETS

The statement of unaudited pro forma adjusted net tangible assets of the Group prepared in accordance with paragraph 31 of Chapter 7 of the GEM Listing Rules is set out below to illustrate the effect of the Placing on the audited consolidated net tangible assets of the Group as if the Placing had taken place on 30 June 2011.

The statement of unaudited pro forma adjusted net tangible assets of the Group has been prepared for illustrative purposes only and, because of its nature, may not give a true picture of the financial position of the Group following the Placing.

The following statement of unaudited pro forma adjusted net tangible assets of the Group is based on the audited consolidated net tangible assets of the Group attributable to the owners of the Company as at 30 June 2011 as shown in the accountants' report of the financial information of the Group, the text of which is set out in Appendix I to this prospectus, and adjusted as follows:

	Audited consolidated net tangible assets of the Group attributable to the owners of the Company as at 30 June 2011 <i>HK\$'000</i> <i>(Note a)</i>	Estimated net proceeds from the Placing <i>HK\$'000</i> <i>(Note b)</i>	Unaudited pro forma adjusted net tangible assets of the Group attributable to the owners of the Company <i>HK\$'000</i>	Unaudited pro forma adjusted net tangible assets per Share <i>HK\$</i> <i>(Note c)</i>
Based on the Placing Price of HK\$1.10 per Share	<u>99,934</u>	<u>46,291</u>	<u>146,225</u>	<u>0.73</u>
Based on the Placing Price of HK\$1.30 per Share	<u>99,934</u>	<u>55,940</u>	<u>155,874</u>	<u>0.78</u>

Notes:

- (a) The audited consolidated net tangible assets of the Group attributable to the owners of the Company as at 30 June 2011 has been derived from the net assets of the Group attributable to the owners of the Company as shown in the accountants' report of the financial information of the Group set out in Appendix I to this prospectus.
- (b) The estimated net proceeds from the Placing are based on 50,000,000 shares at the Placing Price of HK\$1.10 and HK\$1.30 per Share, after deduction of estimated related fees and expenses (excluded listing expenses of approximately HK\$3,820,000 charged to profit or loss during the two years ended 31 December 2010 and the six months ended 30 June 2011).
- (c) The number of shares used for the calculation of unaudited pro forma adjusted net tangible assets per Share is based on 200,000,000 shares in issue immediately after the Placing but takes no account of any shares which may be issued upon the exercise of options that may be granted under the Pre-IPO Share Option Scheme and the Share Option Scheme.
- (d) As of 31 August 2011, the Group's property interests were valued by Greater China Appraisal Limited, an independent property valuer, and the relevant property valuation report is set out in Appendix III to this prospectus. The revaluation surplus, representing the excess of market value of the properties over their book value, is approximately HK\$12,813,000. Such revaluation surplus has not been incorporated in the Group's consolidated financial information for the six months ended 30 June 2011 and will not be incorporated in the Group's consolidated financial statements for the year ending 31 December 2011. The above adjustment does not take into account the above revaluation surplus. Had the properties been stated at such valuation, an additional depreciation of approximately HK\$574,000 per annum would have been charged against profit or loss.

B. ACCOUNTANTS' REPORT ON UNAUDITED PRO FORMA FINANCIAL INFORMATION

Deloitte.
德勤

德勤·關黃陳方會計師行
香港金鐘道88號
太古廣場一座35樓

Deloitte Touche Tohmatsu
35/F, One Pacific Place
88 Queenway
Hong Kong

28 October 2011

Accountants' Report on Unaudited Pro Forma Financial Information to the Directors of RENHENG Enterprise Holdings Limited

We report on the unaudited pro forma financial information of RENHENG Enterprise Holdings Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group"), which has been prepared by the directors of the Company for illustrative purposes only, to provide information about how the placing of 50,000,000 shares of HK\$0.01 each in the Company might have affected the financial information presented, for inclusion in part A of Appendix II to the prospectus dated 28 October 2011 (the "Prospectus"). The basis of preparation of the unaudited pro forma financial information is set out in part A of Appendix II to the Prospectus.

Respective responsibilities of directors of the Company and reporting accountants

It is the responsibility solely of the directors of the Company to prepare the unaudited pro forma financial information in accordance with paragraph 31 of Chapter 7 of the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "GEM Listing Rules") and with reference to Accounting Guideline 7 "Preparation of Pro Forma Financial Information for Inclusion in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants.

It is our responsibility to form an opinion, as required by paragraph 31(7) of Chapter 7 of the GEM Listing Rules, on the unaudited pro forma financial information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the unaudited pro forma financial information beyond that owed to those to whom those reports were addressed by us at the dates of their issue.

Basis of opinion

We conducted our engagement in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 300 "Accountants' Reports on Pro Forma Financial Information in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants. Our work consisted primarily of comparing the unadjusted financial information with source documents, considering the evidence supporting the adjustments and discussing the unaudited pro forma financial information with the directors of the Company. This engagement did not involve independent examination of any of the underlying financial information.

We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the unaudited pro forma financial information has been properly compiled by the directors of the Company on the basis stated, that such basis is consistent with the accounting policies of the Group and that the adjustments are appropriate for the purpose of the unaudited pro forma financial information as disclosed pursuant to paragraph 31(1) of Chapter 7 of the GEM Listing Rules.

The unaudited pro forma financial information is for illustrative purposes only, based on the judgements and assumptions of the directors of the Company, and, because of its hypothetical nature, does not provide any assurance or indication that any event will take place in future and may not be indicative of the financial position of the Group as at 30 June 2011 or any future date.

Opinion

In our opinion:

- a) the unaudited pro forma financial information has been properly compiled by the directors of the Company on the basis stated;
- b) such basis is consistent with the accounting policies of the Group; and
- c) the adjustments are appropriate for the purposes of the unaudited pro forma financial information as disclosed pursuant to paragraph 31(1) of Chapter 7 of the GEM Listing Rules.

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong

GREATER CHINA APPRAISAL LIMITED漢華評值有限公司

Room 2703
Shui On Centre
6-8 Harbour Road
Wanchai
Hong Kong

28 October 2011

The Directors
RENHENG Enterprise Holdings Limited
Room 1303, 13/F.,
Keen Hung Commercial Building,
80 Queen's Road East,
Wanchai, Hong Kong

Dear Sirs,

In accordance with your instructions to value the properties of RENHENG Enterprise Holdings Limited (the "Company") and its subsidiaries (together referred to as the "Group") in the People's Republic of China (the "PRC") and Hong Kong, we confirm that we have carried out inspections, made relevant enquiries and obtained such further information as we consider necessary for the purpose of providing you with our opinion of the capital values of such properties as of 31 August 2011 (referred to as the "date of valuation").

This letter which forms part of our valuation report explains the basis and methodology of valuation, and clarifies our assumptions made, title ship of property and the limiting conditions.

BASIS OF VALUATION

The valuation of such property is our opinion of the market value which we would define as intended to mean "the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion."

VALUATION METHODOLOGY

Due to the nature of buildings and structures constructed, there is no readily identifiable market comparable to the property, we have applied the cost method of valuation in assessing the property in Group I. It is a method of using current replacement costs to arrive at the value to the business in occupation of the property as existing at the date of valuation.

This method of valuation, cost method, is based on an estimate of the market value for the existing use of the land, plus the current gross replacement costs of the improvements, less allowances for physical deterioration and all relevant forms of obsolescence and optimization. The valuation is subject to adequate potential profitability of the concerned business.

The cost method generally furnishes the most reliable indication of value for property in the absence of a known market based on comparable.

ASSUMPTIONS

Our valuation has been made on the assumption that the owner sells the properties in their continued uses and in their existing states without the benefit of any deferred terms contracts, leaseback, joint ventures, management agreements or any similar arrangement which would serve to increase the value of the properties.

Continued use assumes the properties will be used for the purposes for which the properties are designed and built, or to which they are currently adapted. The valuation of the property in continued use does not represent the amount that might be realized from piecemeal disposition of the property on the open market.

For the properties which are held under long term land use rights, we have assumed that the owners of the properties have free and uninterrupted rights to use or transfer the properties for the whole of the unexpired term of the respective land use rights. In our valuation, we have assumed that the properties can be freely disposed of and transferred to third parties on the open market without any additional payment to the relevant government authorities. Unless stated as otherwise, vacant possession is assumed for the property concerned.

We have assumed that all consents, approvals and licences from relevant government authorities for the buildings and structures erected thereon have been granted. Also, we have assumed that all buildings and structures fall within the site are held by the owner or permitted to be occupied by the owner.

It is assumed that all applicable zoning and use regulations and restrictions have been complied with unless nonconformity has been stated, defined and considered in the valuation report. Moreover, it is assumed that the utilization of the land and improvements is within the boundaries of the property described and that no encroachment or trespass exists, unless noted in the report.

No environmental impact study has been ordered or made. Full compliance with applicable national, provincial and local environmental regulations and laws is assumed. In addition, it is assumed that all required licences, consents or other legislative or administrative authority from any local, provincial or national government or private entity or organization either have been or can be obtained or renewed for any use which the report covers.

Other special assumptions of each property, if any, have been stated out in the footnotes of the valuation certificate.

TITLESHP INVESTIGATION

For the property in Group I which is owned by the Group in the PRC, we have been provided with copy of title documents. However, due to the current registration system of the PRC, no investigations have been made for the legal title or any material liabilities attached to the property.

For the properties in Group II which are rented to the Group, we have been provided with copy of tenancy agreements. However, we have not inspected the original documents to verify ownership or to ascertain the existence of any amendments which do not appear on the copies handed to us.

In the course of our valuation, we have relied upon the legal opinions as stated in the title report given by Grandall Legal Group (“The PRC Legal Advisor”) in relation to the legal title to the properties located in the PRC under valuation.

All legal documents disclosed in this report are for reference only and no responsibility is assumed for any legal matters concerning the legal title to the property interest set out in this report.

LIMITING CONDITIONS

We have inspected the exterior and, where possible, the interior of the properties included in the attached valuation certificates. However, no structural survey has been made and we are therefore unable to report as to whether the property is free from rot, infestation or any other structural defects. Also, no tests were carried out on any of the services.

We have not carried out detailed site measurements to verify the correctness of the land or building areas in respect of the properties but have assumed that the areas shown on the legal documents provided to us are correct. Based on our experience of valuation of similar properties, we consider the assumptions so made to be reasonable. All documents and contracts have been used as reference only and all dimensions, measurements and areas are approximations.

No soil investigation has been carried out to determine the suitability of the ground conditions or the services for any property development.

We do not investigate any industrial safety, environmental and health related regulations in association with any particular manufacturing process of the Group. It is assumed that all necessary licences, procedures and measures were implemented in accordance with government legislation and guidance.

Having examined all relevant documentation, we have relied to a very considerable extent on the information provided by the Group and have accepted advice given to us by it on such matters as planning approvals, statutory notices, easements, tenure, occupation, rentals, site and floor areas and in the identification of the property in which the Group has valid interests. We have had no reason to doubt the truth and accuracy of the information provided to us by the Group. We were also advised by the Company that no material factors have been omitted from the information supplied. We consider that we have been provided with sufficient information to reach an informed view, and have no reason to suspect that any material information has been withheld.

No allowance has been made in our valuation for any charges, mortgages or amounts owing on any of the property valued nor for any expenses or taxation which may be incurred in effecting a sale.

Unless otherwise stated, it is assumed that the interests are free of encumbrances, restrictions and outgoing of an onerous nature which could affect their values.

Since the property is located in a relatively under-developed market, the PRC, those assumptions are often based on imperfect market evidence. A range of values may be attributable to the property depending upon the assumptions made. While the valuer has exercised his professional judgment in arriving at the value, report readers are urged to consider carefully the nature of such assumptions which are disclosed in the valuation report and should exercise caution in interpreting the valuation report.

OPINION OF VALUE

Valuation figures of the properties are shown in the attached summary of valuation and their respective valuation certificates.

For the property in Group II which is rented by the Group from independent third party under tenancy agreement, they have no commercial value due to inclusion of non-alienation clause or otherwise due to lack of substantial profit rent or short term nature.

REMARKS

Our valuation has been prepared in accordance with generally accepted valuation procedures and in compliance with the requirements of the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "Rules"), including but are not limited to the provisions of Chapter 8 of the Rules.

In valuing the property interests, we have complied with the requirements contained in the HKIS Valuation Standards on Properties (1st Edition 2005) published by the Hong Kong Institute of Surveyors and effective from 1st January 2005.

Valuation of the property is denominated in Chinese Renminbi (RMB).

We enclosed herewith the summary of valuation and valuation certificates.

This valuation report is issued subject to our General Service Conditions.

Yours faithfully,

For and on behalf of

GREATER CHINA APPRAISAL LIMITED

Nikson Y. T. Ng

MSc MHKIS MRICS

Registered Professional Surveyor(G.P.)

Head of Real Estate & Asset Advisory

Note: Mr. Nikson Y. T. Ng is a Chartered Surveyor and a Registered Professional Surveyor who has over 21 years' experience in valuation of properties in Hong Kong and 5 years' experience in valuation of properties in the PRC.

SUMMARY OF VALUATION

No. Property	Capital Value in existing state as at 31 August 2011
Group I – Property Interests held by the Group in the PRC	
1. Land and buildings located at No.18 North Suzhong Road, Baoying County Yangzhou Jiangsu Province The PRC	RMB39,100,000
Sub-total:	<u>RMB39,100,000</u>
Group II – Property Interests rented to the Group in Hong Kong	
2. Office No.3, 13th Floor, Keen Hung Commercial Building, 80 Queen’s Road East, Wanchai, Hong Kong	no commercial value
Sub-total:	<u>no commercial value</u>
Grand Total:	<u><u>RMB39,100,000</u></u>

VALUATION CERTIFICATE

Group I – Property Interests held by the Group in the PRC

No.	Property	Description and tenure	Particulars of occupancy	Capital Value in existing state as at 31 August 2011																								
1.	Land and buildings located at No.18 North Suzhong Road, Baoying County Yangzhou Jiangsu Province The PRC	<p>The property comprises a parcel of land (the “Land”) with a land area of approximately 62,741.2 square metres and 5 building (the “Buildings”) erected on the Land. The Buildings were completed in 2006.</p> <p>The total gross floor area of the Building is approximately 26,986.14 square metres. Detailed breakdown is shown as follows:</p> <table border="1"> <thead> <tr> <th>Buildings</th> <th>No. of Blocks</th> <th>No. of Storeys</th> <th>Gross Floor Area (sq.m.)</th> </tr> </thead> <tbody> <tr> <td>Factory</td> <td>2</td> <td>2-3</td> <td>23,223.93</td> </tr> <tr> <td>Office</td> <td>1</td> <td>3</td> <td>2,196.61</td> </tr> <tr> <td>Dormitory</td> <td>1</td> <td>4</td> <td>1,524.30</td> </tr> <tr> <td>Guard Room</td> <td>1</td> <td>1</td> <td>41.30</td> </tr> <tr> <td>Total:</td> <td>5</td> <td></td> <td>26,986.14</td> </tr> </tbody> </table> <p>The property is held under a State-owned Land Use Rights Certificate for a term expiring on 6 June 2054 for industrial use.</p>	Buildings	No. of Blocks	No. of Storeys	Gross Floor Area (sq.m.)	Factory	2	2-3	23,223.93	Office	1	3	2,196.61	Dormitory	1	4	1,524.30	Guard Room	1	1	41.30	Total:	5		26,986.14	<p>Portions of the property with a total gross floor area of approximately 9,840 square metres are currently leased to various tenants at a total monthly rent (of August 2011) of approximately RMB59,040 inclusive of management fee but exclusive water and electricity charge. The lease term will expire on 31 December 2012.</p> <p>The remaining portions of the property were occupied by Baoying Renheng for production, storage, dormitory and ancillary office purposes.</p>	RMB39,100,000
Buildings	No. of Blocks	No. of Storeys	Gross Floor Area (sq.m.)																									
Factory	2	2-3	23,223.93																									
Office	1	3	2,196.61																									
Dormitory	1	4	1,524.30																									
Guard Room	1	1	41.30																									
Total:	5		26,986.14																									

Notes:

- (i) According to a State-owned Land Use Rights Certificate (Bao Guo Yong (2007) Di. No. 511) issued by People’s Government of Baoying County dated 19 September 2007, the land use rights of the Land was held by Bao Ying Ren Heng Industrial Co., Ltd. (“Baoying Renheng”, a wholly owned subsidiary of the Company) for a term expiring on 6 June 2054 for industrial use.
- (ii) According to two sets of Building Ownership Certificate (Bao Fang Quan Zheng An Yi Zi Di No. 209439 and 217745) issued by People’s Government of Baoying County, the building ownership of the Buildings is held by Baoying Renheng.
- (iii) In our valuation, we have assumed that the property interest can be freely disposed of and transferred to third parties on the open market without any additional payment to the relevant government authorities.
- (iv) Opinions of the PRC Legal Advisor are summarized as follows:
 - (a) Baoying Renheng has obtained a State-owned Land Use Rights Certificate dated 19 September 2007 by which the land use rights of the Land has been granted to Baoying Renheng for industrial use with land use rights term expiring on 6 June 2054.

- (b) Baoying Renheng has obtained two sets of Building Ownership Certificate in respect of the Buildings.
- (c) Baoying Renheng is the legal holder of the land use rights of the Land and the building ownership rights of the Buildings. During the term of the land use rights, Baoying Renheng has the right to use, occupy, transfer, lease or mortgage the Land and the Buildings.
- (d) No mortgages or other encumbrances over the Land and the Buildings are observed.
- (e) The tenancy agreements are legal, valid and binding.
- (f) The tenancy agreements have been registered at Baoying Real Estate Administration Authority.

Group II – Property Interests rented to the Group in Hong Kong

No.	Property	Descriptions and Occupancy	Capital Value in existing state as at 31 August 2011
2.	Office No.3, 13th Floor, Keen Hung Commercial Building, 80 Queen's Road East, Wanchai, Hong Kong	<p>The property comprises an office unit within a 24-storey commercial building completed in 1998.</p> <p>The gross floor area of the property is approximately 60.94 square meters (656 square feet).</p> <p>The property is rented to the Group under a tenancy agreement for a term of 2 years commencing from 17 January 2011 and expiring on 16 January 2013 at a monthly rent of HK\$13,770 inclusive of rates and management fee.</p> <p>The tenancy is not assignable.</p> <p>The property is occupied by the Group as an office.</p>	no commercial value

(b) Power to dispose of the assets of the Company or any subsidiary

The management of the business of the Company shall be vested in the Directors who, in addition to the powers and authorities by the Articles of Association expressly conferred upon them, may exercise all such powers and do all such acts and things as may be exercised or done or approved by the Company and are not by the Articles of Association or the Companies Law expressly directed or required to be exercised or done by the Company in general meeting, but subject nevertheless to the provisions of the Companies Law and of the Articles of Association and to any regulation from time to time made by the Company in general meeting not being inconsistent with such provisions or the Articles of Association, provided that no regulation so made shall invalidate any prior act of the Directors which would have been valid if such regulation had not been made.

(c) Compensation or payment for loss of office

Payment to any Director or past Director of any sum by way of compensation for loss of office or as consideration for or in connection with his retirement from office (not being a payment to which the Director is contractually entitled) must first be approved by the Company in general meeting.

(d) Loans to Directors

There are provisions in the Articles of Association prohibiting the making of loans to Directors and associates which are equivalent to the restrictions imposed by the Companies Ordinance.

(e) Financial assistance to purchase Shares

Subject to all applicable laws, the Company may give financial assistance to Directors and employees of the Company, its subsidiaries or any holding company or any subsidiary of such holding company in order that they may buy shares in the Company or any such subsidiary or holding company. Further, subject to all applicable laws, the Company may give financial assistance to a trustee for the acquisition of shares in the Company or shares in any such subsidiary or holding company to be held for the benefit of employees of the Company, its subsidiaries, any holding company of the Company or any subsidiary of any such holding company (including salaried Directors).

(f) Disclosure of interest in contracts with the Company or any of its subsidiaries

No Director or proposed Director shall be disqualified by his office from contracting with the Company either as vendor, purchaser or otherwise nor shall any such contract or any contract or arrangement entered into by or on behalf of the Company with any

person, company or partnership of or in which any Director shall be a member or otherwise interested be capable on that account of being avoided, nor shall any Director so contracting or being any member or so interested be liable to account to the Company for any profit so realised by any such contract or arrangement by reason only of such Director holding that office or the fiduciary relationship thereby established, provided that such Director shall, if his interest in such contract or arrangement is material, declare the nature of his interest at the earliest meeting of the board of Directors at which it is practicable for him to do so, either specifically or by way of a general notice stating that, by reason of the facts specified in the notice, he is to be regarded as interested in any contracts of a specified description which may be made by the Company.

A Director shall not be entitled to vote on (nor shall he be counted in the quorum in relation to) any resolution of the Directors in respect of any contract or arrangement or any other proposal in which the Director or any of his associates has any material interest, and if he shall do so his vote shall not be counted (nor is he to be counted in the quorum for the resolution), but this prohibition shall not apply to any of the following matters, namely:

- (i) the giving to such Director or any of his associates of any security or indemnity in respect of money lent or obligations incurred by him or any of them at the request of or for the benefit of the Company or any of its subsidiaries;
- (ii) the giving of any security or indemnity to a third party in respect of a debt or obligation of the Company or any of its subsidiaries for which the Director or any of his associates has himself/themselves assumed responsibility in whole or in part and whether alone or jointly under a guarantee or indemnity or by the giving of security;
- (iii) any proposal concerning an offer of shares, debentures or other securities of or by the Company or any other company which the Company may promote or be interested in for subscription or purchase where the Director or any of his associates is/are or is/are to be interested as a participant in the underwriting or sub-underwriting of the offer;
- (iv) any proposal concerning any other company in which the Director or any of his associates is/are interested only, whether directly or indirectly, as an officer, executive or shareholder or in which the Director or any of his associates is/are beneficially interested in shares of that company, provided that the Director and any of his associates, are not in aggregate beneficially interested in five per cent. or more of the issued shares of any class of such company (or of any third company through which his interest or that of any of his associates is derived) or of the voting rights;

- (v) any proposal or arrangement concerning the benefit of employees of the Company or any of its subsidiaries including:
 - (A) the adoption, modification or operation of any employees' share scheme or any share incentive scheme or share option scheme under which the Director or any of his associates may benefit;
 - (B) the adoption, modification or operation of a pension or provident fund or retirement, death or disability benefits scheme which relates both to Directors, their associates and employees of the Company or any of its subsidiaries and does not provide in respect of any Director or any of his associates as such any privilege or advantage not generally accorded to the class of persons to which such scheme or fund relates; and
- (vi) any contract or arrangement in which the Director or any of his associates is/are interested in the same manner as other holders of shares or debentures or other securities of the Company by virtue only of his/their interest in shares or debentures or other securities of the Company.

(g) Remuneration

The Directors shall be entitled to receive by way of remuneration for their services such sum as shall from time to time be determined by the Directors, or the Company in general meeting, as the case may be, such sum (unless otherwise directed by the resolution by which it is determined) to be divided amongst the Directors in such proportions and in such manner as they may agree, or failing agreement, equally, except that in such event any Director holding office for less than the whole of the relevant period in respect of which the remuneration is paid shall only rank in such division in proportion to the time during such period for which he has held office. Such remuneration shall be in addition to any other remuneration to which a Director who holds any salaried employment or office in the Company may be entitled by reason of such employment or office.

The Directors shall also be entitled to be paid all expenses, including travel expenses, reasonably incurred by them in or in connection with the performance of their duties as Directors including their expenses of travelling to and from board meetings, committee meetings or general meetings or otherwise incurred whilst engaged on the business of the Company or in the discharge of their duties as Directors.

The Directors may grant special remuneration to any Director who shall perform any special or extra services at the request of the Company. Such special remuneration may be made payable to such Director in addition to or in substitution for his ordinary remuneration as a Director, and may be made payable by way of salary, commission or participation in profits or otherwise as may be agreed.

The remuneration of an executive Director or a Director appointed to any other office in the management of the Company shall from time to time be fixed by the Directors and may be by way of salary, commission, or participation in profits or otherwise or by all or any of those modes and with such other benefits (including share option and/or pension and/or gratuity and/or other benefits on retirement) and allowances as the Directors may from time to time decide. Such remuneration shall be in addition to such remuneration as the recipient may be entitled to receive as a Director.

(h) Retirement, appointment and removal

The Directors shall have power at any time and from time to time to appoint any person to be a Director, either to fill a casual vacancy or as an addition to the existing Directors. Any Director so appointed shall hold office only until the next annual general meeting of the Company and shall then be eligible for re-election at that meeting.

The Company may by ordinary resolution remove any Director (including a Managing Director or other executive Director) before the expiration of his period of office notwithstanding anything in the Articles of Association or in any agreement between the Company and such Director (but without prejudice to any claim for compensation or damages payable to him in respect of the termination of his appointment as Director or of any other appointment or office as a result of the termination of his appointment as Director). The Company may by ordinary resolution appoint another person in his place. Any Director so appointed shall hold office during such time only as the Director in whose place he is appointed would have held the same if he had not been removed. The Company may also by ordinary resolution elect any person to be a Director, either to fill a casual vacancy or as an addition to the existing Directors. Any Director so appointed shall hold office only until the next following annual general meeting of the Company and shall then be eligible for re-election. No person shall, unless recommended by the Directors, be eligible for election to the office of Director at any general meeting unless, during the period, which shall be at least seven days, commencing no earlier than the day after the despatch of the notice of the meeting appointed for such election and ending no later than seven days prior to the date of such meeting, there has been given to the Secretary of the Company notice in writing by a member of the Company (not being the person to be proposed) entitled to attend and vote at the meeting for which such notice is given of his intention to propose such person for election and also notice in writing signed by the person to be proposed of his willingness to be elected.

There is no shareholding qualification for Directors nor is there any specified age limit for Directors.

The office of a Director shall be vacated:

- (i) if he resigns his office by notice in writing to the Company at its registered office or its principal office in Hong Kong;

- (ii) if an order is made by any competent court or official on the grounds that he is or may be suffering from mental disorder or is otherwise incapable of managing his affairs and the Directors resolve that his office be vacated;
- (iii) if, without leave, he is absent from meetings of the Directors (unless an alternate Director appointed by him attends) for 12 consecutive months, and the Directors resolve that his office be vacated;
- (iv) if he becomes bankrupt or has a receiving order made against him or suspends payment or compounds with his creditors generally;
- (v) if he ceases to be or is prohibited from being a Director by law or by virtue of any provision in the Articles of Association;
- (vi) if he is removed from office by notice in writing served upon him signed by not less than three-fourths in number (or, if that is not a round number, the nearest lower round number) of the Directors (including himself) for the time being then in office; or
- (vii) if he shall be removed from office by an ordinary resolution of the members of the Company under the Articles of Association.

At every annual general meeting of the Company one-third of the Directors for the time being, or, if their number is not three or a multiple of three, then the number nearest to, but not less than, one-third, shall retire from office by rotation provided that every Director (including those appointed for a specific term) shall be subject to retirement by rotation at least once every three years. A retiring Director shall retain office until the close of the meeting at which he retires and shall be eligible for re-election thereat. The Company at any annual general meeting at which any Directors retire may fill the vacated office by electing a like number of persons to be Directors.

(i) *Borrowing powers*

The Directors may from time to time at their discretion exercise all the powers of the Company to raise or borrow or to secure the payment of any sum or sums of money for the purposes of the Company and to mortgage or charge its undertaking, property and assets (present and future) and uncalled capital or any part thereof.

The rights of the Directors to exercise these powers may only be varied by a special resolution.

(j) *Proceedings of the Board*

The Directors may meet together for the despatch of business, adjourn and otherwise regulate their meetings and proceedings as they think fit in any part of the world. Questions arising at any meeting shall be determined by a majority of votes. In the case of an equality of votes, the chairman of the meeting shall have a second or casting vote.

2.3 Alteration to constitutional documents

No alteration or amendment to the Memorandum or Articles of Association may be made except by special resolution.

2.4 Variation of rights of existing shares or classes of shares

If at any time the share capital of the Company is divided into different classes of shares, all or any of the rights attached to any class of shares for the time being issued (unless otherwise provided for in the terms of issue of the shares of that class) may, subject to the provisions of the Companies Law, be varied or abrogated either with the consent in writing of the holders of not less than three-fourths in nominal value of the issued shares of that class or with the sanction of a special resolution passed at a separate meeting of the holders of the shares of that class. To every such separate meeting all the provisions of the Articles of Association relating to general meetings shall mutatis mutandis apply, but so that the quorum for the purposes of any such separate meeting and of any adjournment thereof shall be a person or persons together holding (or representing by proxy or duly authorised representative) at the date of the relevant meeting not less than one-third in nominal value of the issued shares of that class.

The special rights conferred upon the holders of shares of any class shall not, unless otherwise expressly provided in the rights attaching to or the terms of issue of such shares, be deemed to be varied by the creation or issue of further shares ranking *pari passu* therewith.

2.5 Alteration of Capital

The Company in general meeting may, from time to time, whether or not all the shares for the time being authorised shall have been issued and whether or not all the shares for the time being issued shall have been fully paid up, by ordinary resolution, increase its share capital by the creation of new shares, such new capital to be of such amount and to be divided into shares of such respective amounts as the resolution shall prescribe.

The Company may from time to time by ordinary resolution:

- (a) consolidate and divide all or any of its share capital into shares of larger amount than its existing shares. On any consolidation of fully paid shares and division into shares of larger amount, the Directors may settle any difficulty which may arise as they think expedient and in particular (but without prejudice to the generality of the

foregoing) may as between the holders of shares to be consolidated determine which particular shares are to be consolidated into each consolidated share, and if it shall happen that any person shall become entitled to fractions of a consolidated share or shares, such fractions may be sold by some person appointed by the Directors for that purpose and the person so appointed may transfer the shares so sold to the purchaser thereof and the validity of such transfer shall not be questioned, and so that the net proceeds of such sale (after deduction of the expenses of such sale) may either be distributed among the persons who would otherwise be entitled to a fraction or fractions of a consolidated share or shares rateably in accordance with their rights and interests or may be paid to the Company for the Company's benefit;

- (b) cancel any shares which at the date of the passing of the resolution have not been taken or agreed to be taken by any person, and diminish the amount of its share capital by the amount of the shares so cancelled subject to the provisions of the Companies Law; and
- (c) sub-divide its shares or any of them into shares of smaller amount than is fixed by the Memorandum of Association, subject nevertheless to the provisions of the Companies Law, and so that the resolution whereby any share is sub-divided may determine that, as between the holders of the shares resulting from such sub-division, one or more of the shares may have any such preferred or other special rights, over, or may have such deferred rights or be subject to any such restrictions as compared with the others as the company has power to attach to unissued or new shares.

The Company may by special resolution reduce its share capital or any capital redemption reserve in any manner authorised and subject to any conditions prescribed by the Companies Law.

2.6 Special resolution – majority required

A “special resolution” is defined in the Articles of Association to have the meaning ascribed thereto in the Companies Law, for which purpose, the requisite majority shall be not less than three-fourths of the votes of such members of the Company as, being entitled to do so, vote in person or, in the case of corporations, by their duly authorised representatives or, where proxies are allowed, by proxy at a general meeting of which notice specifying the intention to propose the resolution as a special resolution has been duly given and includes a special resolution approved in writing by all of the members of the Company entitled to vote at a general meeting of the Company in one or more instruments each signed by one or more of such members, and the effective date of the special resolution so adopted shall be the date on which the instrument or the last of such instruments (if more than one) is executed.

In contrast, an “ordinary resolution” is defined in the Articles of Association to mean a resolution passed by a simple majority of the votes of such members of the Company as, being entitled to do so, vote in person or, in the case of corporations, by their duly authorised representatives or, where proxies are allowed, by proxy at a general meeting held in accordance with the Articles of Association and includes an ordinary resolution approved in writing by all the members of the Company aforesaid.

2.7 Voting rights

Subject to any special rights, privileges or restrictions as to voting for the time being attached to any class or classes of shares, at any general meeting on a poll every member present in person (or, in the case of a member being a corporation, by its duly authorised representative) or by proxy shall have one vote for each share registered in his name in the register of members of the Company.

Where any member of the Company is, under the Listing Rules, required to abstain from voting on any particular resolution or is restricted to voting only for or only against any particular resolution, any votes cast by or on behalf of such member in contravention of such requirement or restriction shall not be counted.

In the case of joint registered holders of any share, any one of such persons may vote at any meeting, either personally or by proxy, in respect of such share as if he were solely entitled thereto; but if more than one of such joint holders be present at any meeting personally or by proxy, that one of the said persons so present being the most or, as the case may be, the more senior shall alone be entitled to vote in respect of the relevant joint holding and, for this purpose, seniority shall be determined by reference to the order in which the names of the joint holders stand on the register in respect of the relevant joint holding.

A member of the Company in respect of whom an order has been made by any competent court or official on the grounds that he is or may be suffering from mental disorder or is otherwise incapable of managing his affairs may vote by any person authorised in such circumstances to do so and such person may vote by proxy.

Save as expressly provided in the Articles of Association or as otherwise determined by the Directors, no person other than a member of the Company duly registered and who shall have paid all sums for the time being due from him payable to the Company in respect of his shares shall be entitled to be present or to vote (save as proxy for another member of the Company), or to be counted in a quorum, either personally or by proxy at any general meeting.

At any general meeting a resolution put to the vote of the meeting is to be decided by way of a poll.

If a recognised clearing house (or its nominee) is a member of the Company it may authorise such person or persons as it thinks fit to act as its proxy(ies) or representative(s) at any general meeting of the Company or at any general meeting of any class of members of the Company provided that, if more than one person is so authorised, the authorisation shall specify the number and class of shares in respect of which each such person is so authorised. A person authorised pursuant to this provision shall be entitled to exercise the same rights and powers on behalf of the recognised clearing house (or its nominee) which he represents as that recognised clearing house (or its nominee) could exercise as if it were an individual member of the Company holding the number and class of shares specified in such authorisation.

2.8 Annual general meetings

The Company shall in each year hold a general meeting as its annual general meeting in addition to any other general meeting in that year and shall specify the meeting as such in the notice calling it; and not more than 15 months (or such longer period as the Stock Exchange may authorise) shall elapse between the date of one annual general meeting of the Company and that of the next.

2.9 Accounts and audit

The Directors shall cause to be kept such books of account as are necessary to give a true and fair view of the state of the Company's affairs and to show and explain its transactions and otherwise in accordance with the Companies Law.

The Directors shall from time to time determine whether, and to what extent, and at what times and places and under what conditions or regulations, the accounts and books of the Company, or any of them, shall be open to the inspection of members of the Company (other than officers of the Company) and no such member shall have any right of inspecting any accounts or books or documents of the Company except as conferred by the Companies Law or any other relevant law or regulation or as authorised by the Directors or by the Company in general meeting.

The Directors shall, commencing with the first annual general meeting, cause to be prepared and to be laid before the members of the Company at every annual general meeting a profit and loss account for the period, in the case of the first account, since the incorporation of the Company and, in any other case, since the preceding account, together with a balance sheet as at the date at which the profit and loss account is made up and a Director's report with respect to the profit or loss of the Company for the period covered by the profit and loss account and the state of the Company's affairs as at the end of such period, an auditor's report on such accounts and such other reports and accounts as may be required by law. Copies of those documents to be laid before the members of the Company at an annual general meeting shall not less than 21 clear days before the date of the meeting, be sent in the manner in which notices may be served by the Company as provided in the Articles of Association to every member of

the Company and every holder of debentures of the Company provided that the Company shall not be required to send copies of those documents to any person of whose address the Company is not aware or to more than one of the joint holders of any shares or debentures.

The Company shall at any annual general meeting appoint an auditor or auditors of the Company who shall hold office until the next annual general meeting. The remuneration of the auditors shall be fixed by the Company at the annual general meeting at which they are appointed provided that in respect of any particular year the Company in general meeting may delegate the fixing of such remuneration to the Directors.

2.10 Notice of meetings and business to be conducted thereat

An annual general meeting and any extraordinary general meeting called for the passing of a special resolution shall be called by notice of not less than 21 clear days and any other extraordinary general meeting shall be called by not less than 14 clear days. The notice shall be inclusive of the day on which it is served or deemed to be served and of the day for which it is given, and shall specify the time, place and agenda of the meeting, particulars of the resolutions to be considered at the meeting and, in the case of special business, the general nature of that business. The notice convening an annual general meeting shall specify the meeting as such, and the notice convening a meeting to pass a special resolution shall specify the intention to propose the resolution as a special resolution. Notice of every general meeting shall be given to the auditors and all members of the Company (other than those who, under the provisions of the Articles of Association or the terms of issue of the shares they hold, are not entitled to receive such notice from the Company).

Notwithstanding that a meeting of the Company is called by shorter notice than that mentioned above, it shall be deemed to have been duly called if it is so agreed:

- (a) in the case of a meeting called as an annual general meeting, by all members of the Company entitled to attend and vote thereat or their proxies; and
- (b) in the case of any other meeting, by a majority in number of the members having a right to attend and vote at the meeting, being a majority together holding not less than 95 per cent. in nominal value of the shares giving that right.

All business shall be deemed special that is transacted at an extraordinary general meeting and also all business shall be deemed special that is transacted at an annual general meeting with the exception of the following, which shall be deemed ordinary business:

- (a) the declaration and sanctioning of dividends;
- (b) the consideration and adoption of the accounts and balance sheets and the reports of the Directors and the auditors and other documents required to be annexed to the balance sheet;

- (c) the election of Directors in place of those retiring;
- (d) the appointment of auditors;
- (e) the fixing of, or the determining of the method of fixing of, the remuneration of the Directors and of the auditors;
- (f) the granting of any mandate or authority to the Directors to offer, allot, grant options over or otherwise dispose of the unissued shares of the Company representing not more than 20 per cent. (or such other percentage as may from time to time be specified in the Listing Rules) in nominal value of its then existing issued share capital and the number of any securities repurchased pursuant to sub-paragraph (g) below; and
- (g) the granting of any mandate or authority to the Directors to repurchase securities of the Company.

2.11 Transfer of Shares

Transfers of shares may be effected by an instrument of transfer in the usual common form or in such other form as the Directors may approve which is consistent with the standard form of transfer as prescribed by the Stock Exchange.

The instrument of transfer shall be executed by or on behalf of the transferor and, unless the Directors otherwise determine, the transferee, and the transferor shall be deemed to remain the holder of the share until the name of the transferee is entered in the register of members of the Company in respect thereof. All instruments of transfer shall be retained by the Company.

The Directors may refuse to register any transfer of any share which is not fully paid up or on which the Company has a lien. The Directors may also decline to register any transfer of any shares unless:

- (a) the instrument of transfer is lodged with the Company accompanied by the certificate for the shares to which it relates (which shall upon the registration of the transfer be cancelled) and such other evidence as the Directors may reasonably require to show the right of the transferor to make the transfer;
- (b) the instrument of transfer is in respect of only one class of shares;
- (c) the instrument of transfer is properly stamped (in circumstances where stamping is required);
- (d) in the case of a transfer to joint holders, the number of joint holders to whom the share is to be transferred does not exceed four;

- (e) the shares concerned are free of any lien in favour of the Company; and
- (f) a fee of such maximum as the Stock Exchange may from time to time determine to be payable (or such lesser sum as the Directors may from time to time require) is paid to the Company in respect thereof.

If the Directors refuse to register a transfer of any share they shall, within two months after the date on which the instrument of transfer was lodged with the Company, send to each of the transferor and the transferee notice of such refusal.

The registration of transfers may, on 14 days' notice being given by advertisement published on the Stock Exchange's website, or, subject to the Listing Rules, by electronic communication in the manner in which notices may be served by the Company by electronic means as provided in the Articles of Association or by advertisement published in the newspapers, be suspended and the register of members of the Company closed at such times for such periods as the Directors may from time to time determine, provided that the registration of transfers shall not be suspended or the register closed for more than 30 days in any year (or such longer period as the members of the Company may by ordinary resolution determine provided that such period shall not be extended beyond 60 days in any year).

2.12 Power of the Company to purchase its own Shares

The Company is empowered by the Companies Law and the Articles of Association to purchase its own shares subject to certain restrictions and the Directors may only exercise this power on behalf of the Company subject to the authority of its members in general meeting as to the manner in which they do so and to any applicable requirements imposed from time to time by the Stock Exchange and the Securities and Futures Commission of Hong Kong. Shares which have been repurchased will be treated as cancelled upon the repurchase, unless the directors resolve prior to the repurchase that upon the repurchase, the shares shall be held in the name of the Company as treasury shares.

Where the Company purchases for redemption a redeemable share, purchases not made through the market or by tender shall be limited to a maximum price, and if purchases are by tender, tenders shall be available to all members alike. The purchase or redemption of any share shall not be deemed to give rise to the purchase or redemption of any other share.

2.13 Power of any subsidiary of the Company to own Shares

There are no provisions in the Articles of Association relating to the ownership of shares by a subsidiary.

2.14 Dividends and other methods of distributions

Subject to the Companies Law and Articles of Association, the Company in general meeting may declare dividends in any currency but no dividends shall exceed the amount recommended by the Directors. No dividend may be declared or paid other than out of profits and reserves of the Company lawfully available for distribution, including share premium.

Unless and to the extent that the rights attached to any shares or the terms of issue thereof otherwise provide, all dividends shall (as regards any shares not fully paid throughout the period in respect of which the dividend is paid) be apportioned and paid pro rata according to the amounts paid up on the shares during any portion or portions of the period in respect of which the dividend is paid. For these purposes no amount paid up on a share in advance of calls shall be treated as paid up on the share.

The Directors may from time to time pay to the members of the Company such interim dividends as appear to the Directors to be justified by the profits of the Company. The Directors may also pay half-yearly or at other intervals to be selected by them at a fixed rate if they are of the opinion that the profits available for distribution justify the payment.

The Directors may retain any dividends or other moneys payable on or in respect of a share upon which the Company has a lien, and may apply the same in or towards satisfaction of the debts, liabilities or engagements in respect of which the lien exists. The Directors may also deduct from any dividend or other monies payable to any member of the Company all sums of money (if any) presently payable by him to the Company on account of calls, instalments or otherwise.

No dividend shall carry interest against the Company.

Whenever the Directors or the Company in general meeting have resolved that a dividend be paid or declared on the share capital of the Company, the Directors may further resolve: (a) that such dividend be satisfied wholly or in part in the form of an allotment of shares credited as fully paid up on the basis that the shares so allotted are to be of the same class as the class already held by the allottee, provided that the members of the Company entitled thereto will be entitled to elect to receive such dividend (or part thereof) in cash in lieu of such allotment; or (b) that the members of the Company entitled to such dividend will be entitled to elect to receive an allotment of shares credited as fully paid up in lieu of the whole or such part of the dividend as the Directors may think fit on the basis that the shares so allotted are to be of the same class as the class already held by the allottee. The Company may upon the recommendation of the Directors by ordinary resolution resolve in respect of any one particular dividend of the Company that notwithstanding the foregoing a dividend may be satisfied wholly in the form of an allotment of shares credited as fully paid without offering any right to members of the Company to elect to receive such dividend in cash in lieu of such allotment.

Any dividend, interest or other sum payable in cash to a holder of shares may be paid by cheque or warrant sent through the post addressed to the registered address of the member of the Company entitled, or in the case of joint holders, to the registered address of the person whose name stands first in the register of members of the Company in respect of the joint holding or to such person and to such address as the holder or joint holders may in writing direct. Every cheque or warrant so sent shall be made payable to the order of the holder or, in the case of joint holders, to the order of the holder whose name stands first on the register of members of

the Company in respect of such shares, and shall be sent at his or their risk and the payment of any such cheque or warrant by the bank on which it is drawn shall operate as a good discharge to the Company in respect of the dividend and/or bonus represented thereby, notwithstanding that it may subsequently appear that the same has been stolen or that any endorsement thereon has been forged. The Company may cease sending such cheques for dividend entitlements or dividend warrants by post if such cheques or warrants have been left uncashed on two consecutive occasions. However, the Company may exercise its power to cease sending cheques for dividend entitlements or dividend warrants after the first occasion on which such a cheque or warrant is returned undelivered. Any one of two or more joint holders may give effectual receipts for any dividends or other moneys payable or property distributable in respect of the shares held by such joint holders.

Any dividend unclaimed for six years from the date of declaration of such dividend may be forfeited by the Directors and shall revert to the Company.

The Directors may, with the sanction of the members of the Company in general meeting, direct that any dividend be satisfied wholly or in part by the distribution of specific assets of any kind, and in particular of paid up shares, debentures or warrants to subscribe securities of any other company, and where any difficulty arises in regard to such distribution the Directors may settle it as they think expedient, and in particular may disregard fractional entitlements, round the same up or down or provide that the same shall accrue to the benefit of the Company, and may fix the value for distribution of such specific assets and may determine that cash payments shall be made to any members of the Company upon the footing of the value so fixed in order to adjust the rights of all parties, and may vest any such specific assets in trustees as may seem expedient to the Directors.

2.15 Proxies

Any member of the Company entitled to attend and vote at a meeting of the Company shall be entitled to appoint another person who must be an individual as his proxy to attend and vote instead of him and a proxy so appointed shall have the same right as the member to speak at the meeting. A proxy need not be a member of the Company.

Instruments of proxy shall be in common form or in such other form as the Directors may from time to time approve provided that it shall enable a member to instruct his proxy to vote in favour of or against (or in default of instructions or in the event of conflicting instructions, to exercise his discretion in respect of) each resolution to be proposed at the meeting to which the form of proxy relates. The instrument of proxy shall be deemed to confer authority to vote on any amendment of a resolution put to the meeting for which it is given as the proxy thinks fit. The instrument of proxy shall, unless the contrary is stated therein, be valid as well for any adjournment of the meeting as for the meeting to which it relates provided that the meeting was originally held within 12 months from such date.

The instrument appointing a proxy shall be in writing under the hand of the appointor or his attorney authorised in writing, or if the appointor is a corporation either under its seal or under the hand of an officer, attorney or other person authorised to sign the same.

The instrument appointing a proxy and (if required by the Directors) the power of attorney or other authority (if any) under which it is signed, or a notarially certified copy of such power or authority, shall be delivered at the registered office of the Company (or at such other place as may be specified in the notice convening the meeting or in any notice of any adjournment or, in either case, in any document sent therewith) not less than 48 hours before the time appointed for holding the meeting or adjourned meeting at which the person named in the instrument proposes to vote or, in the case of a poll taken subsequently to the date of a meeting or adjourned meeting, not less than 48 hours before the time appointed for the taking of the poll and in default the instrument of proxy shall not be treated as valid. No instrument appointing a proxy shall be valid after the expiration of 12 months from the date named in it as the date of its execution. Delivery of any instrument appointing a proxy shall not preclude a member of the Company from attending and voting in person at the meeting or poll concerned and, in such event, the instrument appointing a proxy shall be deemed to be revoked.

2.16 Calls on Shares and forfeiture of Shares

The Directors may from time to time make calls upon the members of the Company in respect of any moneys unpaid on their shares (whether on account of the nominal amount of the shares or by way of premium or otherwise) and not by the conditions of allotment thereof made payable at fixed times and each member of the Company shall (subject to the Company serving upon him at least 14 days' notice specifying the time and place of payment and to whom such payment shall be made) pay to the person at the time and place so specified the amount called on his shares. A call may be revoked or postponed as the Directors may determine. A person upon whom a call is made shall remain liable on such call notwithstanding the subsequent transfer of the shares in respect of which the call was made.

A call may be made payable either in one sum or by instalments and shall be deemed to have been made at the time when the resolution of the Directors authorising the call was passed. The joint holders of a share shall be jointly and severally liable to pay all calls and instalments due in respect of such share or other moneys due in respect thereof.

If a sum called in respect of a share shall not be paid before or on the day appointed for payment thereof, the person from whom the sum is due shall pay interest on the sum from the day appointed for payment thereof to the time of actual payment at such rate, not exceeding 15 per cent. per annum, as the Directors may determine, but the Directors shall be at liberty to waive payment of such interest wholly or in part.

If any call or instalment of a call remains unpaid on any share after the day appointed for payment thereof, the Directors may at any time during such time as any part thereof remains unpaid serve a notice on the holder of such shares requiring payment of so much of the call or instalment as is unpaid together with any interest which may be accrued and which may still accrue up to the date of actual payment.

The notice shall name a further day (not being less than 14 days from the date of service of the notice) on or before which, and the place where, the payment required by the notice is to be made, and shall state that in the event of non-payment at or before the time and at the place appointed, the shares in respect of which such call was made or instalment is unpaid will be liable to be forfeited.

If the requirements of such notice are not complied with, any share in respect of which such notice has been given may at any time thereafter, before payment of all calls or instalments and interest due in respect thereof has been made, be forfeited by a resolution of the Directors to that effect. Such forfeiture shall include all dividends and bonuses declared in respect of the forfeited shares and not actually paid before the forfeiture. A forfeited share shall be deemed to be the property of the Company and may be sold, re-allotted or otherwise disposed of.

A person whose shares have been forfeited shall cease to be a member of the Company in respect of the forfeited shares but shall, notwithstanding the forfeiture, remain liable to pay to the Company all moneys which at the date of forfeiture were payable by him to the Company in respect of the shares, together with (if the Directors shall in their discretion so require) interest thereon at such rate not exceeding 15 per cent. per annum as the Directors may prescribe from the date of forfeiture until payment, and the Directors may enforce payment thereof without being under any obligation to make any allowance for the value of the shares forfeited, at the date of forfeiture.

2.17 Inspection of register of members

The register of members of the Company shall be kept in such manner as to show at all times the members of the Company for the time being and the shares respectively held by them. The register may, on 14 days' notice being given by advertisement published on the Stock Exchange's website, or subject to the Listing Rules, by electronic communication in the manner in which notices may be served by the Company by electronic means as provided in the Articles of Association or by advertisement published in the newspapers, be closed at such times and for such periods as the Directors may from time to time determine either generally or in respect of any class of shares, provided that the register shall not be closed for more than 30 days in any year (or such longer period as the members of the Company may by ordinary resolution determine provided that such period shall not be extended beyond 60 days in any year).

Any register of members kept in Hong Kong shall during normal business hours (subject to such reasonable restrictions as the Directors may impose) be open to inspection by any member of the Company without charge and by any other person on payment of such fee not exceeding HK\$2.50 (or such higher amount as may from time to time be permitted under the Listing Rules) as the Directors may determine for each inspection.

2.18 Quorum for meetings and separate class meetings

No business shall be transacted at any general meeting unless a quorum is present when the meeting proceeds to business, but the absence of a quorum shall not preclude the appointment, choice or election of a chairman which shall not be treated as part of the business of the meeting.

Two members of the Company present in person or by proxy shall be a quorum provided always that if the Company has only one member of record the quorum shall be that one member present in person or by proxy.

A corporation being a member of the Company shall be deemed for the purpose of the Articles of Association to be present in person if represented by its duly authorised representative being the person appointed by resolution of the directors or other governing body of such corporation or by power of attorney to act as its representative at the relevant general meeting of the Company or at any relevant general meeting of any class of members of the Company.

The quorum for a separate general meeting of the holders of a separate class of shares of the Company is described in sub-paragraph 2.4 above.

2.19 Rights of minorities in relation to fraud or oppression

There are no provisions in the Articles of Association concerning the rights of minority shareholders in relation to fraud or oppression.

2.20 Procedure on liquidation

If the Company shall be wound up, and the assets available for distribution amongst the members of the Company as such shall be insufficient to repay the whole of the paid up capital, such assets shall be distributed so that, as nearly as may be, the losses shall be borne by the members of the Company in proportion to the capital paid up, or which ought to have been paid up, at the commencement of the winding up on the shares held by them respectively. And if in a winding up the assets available for distribution amongst the members of the Company shall be more than sufficient to repay the whole of the capital paid up at the commencement of the winding up, the excess shall be distributed amongst the members of the Company in proportion to the capital paid up at the commencement of the winding up on the shares held by them respectively. The foregoing is without prejudice to the rights of the holders of shares issued upon special terms and conditions.

If the Company shall be wound up, the liquidator may with the sanction of a special resolution of the Company and any other sanction required by the Companies Law, divide amongst the members of the Company in specie or kind the whole or any part of the assets of the Company (whether they shall consist of property of the same kind or not) and may, for such

purpose, set such value as he deems fair upon any property to be divided as aforesaid and may determine how such division shall be carried out as between the members or different classes of members of the Company. The liquidator may, with the like sanction, vest the whole or any part of such assets in trustees upon such trusts for the benefit of the members of the Company as the liquidator, with the like sanction and subject to the Companies Law, shall think fit, but so that no member of the Company shall be compelled to accept any assets, shares or other securities in respect of which there is a liability.

2.21 Untraceable members

The Company shall be entitled to sell any shares of a member of the Company or the shares to which a person is entitled by virtue of transmission on death or bankruptcy or operation of law if: (i) all cheques or warrants, not being less than three in number, for any sums payable in cash to the holder of such shares have remained uncashed for a period of 12 years; (ii) the Company has not during that time or before the expiry of the three month period referred to in (iv) below received any indication of the whereabouts or existence of the member; (iii) during the 12 year period, at least three dividends in respect of the shares in question have become payable and no dividend during that period has been claimed by the member; and (iv) upon expiry of the 12 year period, the Company has caused an advertisement to be published in the newspapers or subject to the Listing Rules, by electronic communication in the manner in which notices may be served by the Company by electronic means as provided in the Articles of Association, giving notice of its intention to sell such shares and a period of three months has elapsed since such advertisement and the Stock Exchange has been notified of such intention. The net proceeds of any such sale shall belong to the Company and upon receipt by the Company of such net proceeds it shall become indebted to the former member for an amount equal to such net proceeds.

B. SUMMARY OF THE CAYMAN ISLANDS COMPANY LAW AND TAXATION

1 INTRODUCTION

The Companies Law is derived, to a large extent, from the older Companies Acts of England, although there are significant differences between the Companies Law and the current Companies Act of England. Set out below is a summary of certain provisions of the Companies Law, although this does not purport to contain all applicable qualifications and exceptions or to be a complete review of all matters of corporate law and taxation which may differ from equivalent provisions in jurisdictions with which interested parties may be more familiar.

2 INCORPORATION

The Company was incorporated in the Cayman Islands as an exempted company with limited liability on 2 February 2011 under the Companies Law. As such, its operations must be conducted mainly outside the Cayman Islands. The Company is required to file an annual return each year with the Registrar of Companies of the Cayman Islands and pay a fee which is based on the size of its authorised share capital.

3 SHARE CAPITAL

The Companies Law permits a company to issue ordinary shares, preference shares, redeemable shares or any combination thereof.

The Companies Law provides that where a company issues shares at a premium, whether for cash or otherwise, a sum equal to the aggregate amount of the value of the premia on those shares shall be transferred to an account called the “share premium account”. At the option of a company, these provisions may not apply to premia on shares of that company allotted pursuant to any arrangement in consideration of the acquisition or cancellation of shares in any other company and issued at a premium. The Companies Law provides that the share premium account may be applied by a company, subject to the provisions, if any, of its memorandum and articles of association, in such manner as the company may from time to time determine including, but without limitation:

- (a) paying distributions or dividends to members;
- (b) paying up unissued shares of the company to be issued to members as fully paid bonus shares;
- (c) in the redemption and repurchase of shares (subject to the provisions of section 37 of the Companies Law);
- (d) writing-off the preliminary expenses of the company;
- (e) writing-off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company; and
- (f) providing for the premium payable on redemption or purchase of any shares or debentures of the company.

No distribution or dividend may be paid to members out of the share premium account unless immediately following the date on which the distribution or dividend is proposed to be paid the company will be able to pay its debts as they fall due in the ordinary course of business.

The Companies Law provides that, subject to confirmation by the Grand Court of the Cayman Islands, a company limited by shares or a company limited by guarantee and having a share capital may, if so authorised by its articles of association, by special resolution reduce its share capital in any way.

Subject to the detailed provisions of the Companies Law, a company limited by shares or a company limited by guarantee and having a share capital may, if so authorised by its articles of association, issue shares which are to be redeemed or are liable to be redeemed at the option of the company or a shareholder. In addition, such a company may, if authorised to do so by its articles of association, purchase its own shares, including any redeemable shares. The manner of such a

purchase must be authorised either by the articles of association or by an ordinary resolution of the company. The articles of association may provide that the manner of purchase may be determined by the directors of the company. At no time may a company redeem or purchase its shares unless they are fully paid. A company may not redeem or purchase any of its shares if, as a result of the redemption or purchase, there would no longer be any member of the company holding shares. A payment out of capital by a company for the redemption or purchase of its own shares is not lawful unless immediately following the date on which the payment is proposed to be made, the company shall be able to pay its debts as they fall due in the ordinary course of business.

There is no statutory restriction in the Cayman Islands on the provision of financial assistance by a company for the purchase of, or subscription for, its own or its holding company's shares. Accordingly, a company may provide financial assistance if the directors of the company consider, in discharging their duties of care and to act in good faith, for a proper purpose and in the interests of the company, that such assistance can properly be given. Such assistance should be on an arm's-length basis.

4 DIVIDENDS AND DISTRIBUTIONS

With the exception of section 34 of the Companies Law, there are no statutory provisions relating to the payment of dividends. Based upon English case law which is likely to be persuasive in the Cayman Islands in this area, dividends may be paid only out of profits. In addition, section 34 of the Companies Law permits, subject to a solvency test and the provisions, if any, of the company's memorandum and articles of association, the payment of dividends and distributions out of the share premium account (see 3 above for further details).

5 SHAREHOLDERS' SUITS

The Cayman Islands courts can be expected to follow English case law precedents. The rule in *Foss v. Harbottle* (and the exceptions thereto which permit a minority shareholder to commence a class action against or derivative actions in the name of the company to challenge (a) an act which is ultra vires the company or illegal, (b) an act which constitutes a fraud against the minority where the wrongdoers are themselves in control of the company, and (c) an action which requires a resolution with a qualified (or special) majority which has not been obtained) has been applied and followed by the courts in the Cayman Islands.

6 PROTECTION OF MINORITIES

In the case of a company (not being a bank) having a share capital divided into shares, the Grand Court of the Cayman Islands may, on the application of members holding not less than one fifth of the shares of the company in issue, appoint an inspector to examine into the affairs of the company and to report thereon in such manner as the Grand Court shall direct.

Any shareholder of a company may petition the Grand Court of the Cayman Islands which may make a winding up order if the court is of the opinion that it is just and equitable that the company should be wound up.

Claims against a company by its shareholders must, as a general rule, be based on the general laws of contract or tort applicable in the Cayman Islands or their individual rights as shareholders as established by the company's memorandum and articles of association.

The English common law rule that the majority will not be permitted to commit a fraud on the minority has been applied and followed by the courts of the Cayman Islands.

7 DISPOSAL OF ASSETS

The Companies Law contains no specific restrictions on the powers of directors to dispose of assets of a company. As a matter of general law, in the exercise of those powers, the directors must discharge their duties of care and to act in good faith, for a proper purpose and in the interests of the company.

8 ACCOUNTING AND AUDITING REQUIREMENTS

The Companies Law requires that a company shall cause to be kept proper books of account, including, where applicable, material underlying documentation including contracts and invoices, with respect to:

- (a) all sums of money received and expended by the company and the matters in respect of which the receipt and expenditure takes place;
- (b) all sales and purchases of goods by the company; and
- (c) the assets and liabilities of the company.

Proper books of account shall not be deemed to be kept if there are not kept such books as are necessary to give a true and fair view of the state of the company's affairs and to explain its transactions.

9 REGISTER OF MEMBERS

An exempted company may, subject to the provisions of its articles of association, maintain its principal register of members and any branch registers at such locations, whether within or without the Cayman Islands, as its directors may, from time to time, think fit. There is no requirement under the Companies Law for an exempted company to make any returns of members to the Registrar of Companies in the Cayman Islands. The names and addresses of the members are, accordingly, not a matter of public record and are not available for public inspection.

10 INSPECTION OF BOOKS AND RECORDS

Members of a company will have no general right under the Companies Law to inspect or obtain copies of the register of members or corporate records of the company. They will, however, have such rights as may be set out in the company's articles of association.

11 SPECIAL RESOLUTIONS

The Companies Law provides that a resolution is a special resolution when it has been passed by a majority of not less than two-thirds (or such greater number as may be specified in the articles of association of the company) of such members as, being entitled to do so, vote in person or, where proxies are allowed, by proxy at a general meeting of which notice specifying the intention to propose the resolution as a special resolution has been duly given. Written resolutions signed by all the members entitled to vote for the time being of the company may take effect as special resolutions if this is authorised by the articles of association of the company.

12 SUBSIDIARY OWNING SHARES IN PARENT

The Companies Law does not prohibit a Cayman Islands company acquiring and holding shares in its parent company provided its objects so permit. The directors of any subsidiary making such acquisition must discharge their duties of care and to act in good faith, for a proper purpose and in the interests of the subsidiary.

13 MERGERS AND CONSOLIDATIONS

The Companies Law permits mergers and consolidations between Cayman Islands companies and between Cayman Islands companies and non-Cayman Islands companies. For these purposes, (a) "merger" means the merging of two or more constituent companies and the vesting of their undertaking, property and liabilities in one of such companies as the surviving company and (b) a "consolidation" means the combination of two or more constituent companies into a consolidated company and the vesting of the undertaking, property and liabilities of such companies to the consolidated company. In order to effect such a merger or consolidation, the directors of each constituent company must approve a written plan of merger or consolidation, which must then be authorised by either (a) a special resolution of each constituent company or (b) such other authorisation, if any, as may be specified in such constituent company's articles of association. The written plan of merger or consolidation must be filed with the Registrar of Companies together with a declaration as to the solvency of the consolidated or surviving company, a list of the assets and liabilities of each constituent company and an undertaking that a copy of the certificate of merger or consolidation will be given to the members and creditors of each constituent company and that notification of the merger or consolidation will be published in the Cayman Islands Gazette. Dissenting shareholders have the right to be paid the fair value of their shares (which, if not agreed between the parties, will be determined by the Cayman Islands court) if they follow the required procedures, subject to certain exceptions. Court approval is not required for a merger or consolidation which is effected in compliance with these statutory procedures.

14 RECONSTRUCTIONS

There are statutory provisions which facilitate reconstructions and amalgamations approved by a majority in number representing 75% in value of shareholders or creditors, depending on the circumstances, as are present at a meeting called for such purpose and thereafter sanctioned by the Grand Court of the Cayman Islands. Whilst a dissenting shareholder would have the right to express to the Grand Court his view that the transaction for which approval is sought would not provide the shareholders with a fair value for their shares, the Grand Court of the Cayman Islands is unlikely to disapprove the transaction on that ground alone in the absence of evidence of fraud or bad faith on behalf of management and if the transaction were approved and consummated the dissenting shareholder would have no rights comparable to the appraisal rights (i.e. the right to receive payment in cash for the judicially determined value of his shares) ordinarily available, for example, to dissenting shareholders of United States corporations.

15 TAKE-OVERS

Where an offer is made by a company for the shares of another company and, within four months of the offer, the holders of not less than 90% of the shares which are the subject of the offer accept, the offeror may at any time within two months after the expiration of the said four months, by notice require the dissenting shareholders to transfer their shares on the terms of the offer. A dissenting shareholder may apply to the Grand Court of the Cayman Islands within one month of the notice objecting to the transfer. The burden is on the dissenting shareholder to show that the Grand Court should exercise its discretion, which it will be unlikely to do unless there is evidence of fraud or bad faith or collusion as between the offeror and the holders of the shares who have accepted the offer as a means of unfairly forcing out minority shareholders.

16 INDEMNIFICATION

Cayman Islands law does not limit the extent to which a company's articles of association may provide for indemnification of officers and directors, except to the extent any such provision may be held by the Cayman Islands courts to be contrary to public policy (e.g. for purporting to provide indemnification against the consequences of committing a crime).

17 LIQUIDATION

A company is placed in liquidation either by an order of the court or by a special resolution (or, in certain circumstances, an ordinary resolution) of its members. A liquidator is appointed whose duties are to collect the assets of the company (including the amount (if any) due from the contributories (shareholders)), settle the list of creditors and discharge the company's liability to them, rateably if insufficient assets exist to discharge the liabilities in full, and to settle the list of contributories and divide the surplus assets (if any) amongst them in accordance with the rights attaching to the shares.

1. FURTHER INFORMATION ABOUT THE COMPANY AND ITS SUBSIDIARIES**A. Incorporation of the Company**

The Company was incorporated in the Cayman Islands under the Companies Law as an exempted company with limited liability on 2 February 2011. The Company has established a place of business in Hong Kong at Room 1303, 13/F., Keen Hung Commercial Building, 80 Queen's Road East, Wanchai, and was registered in Hong Kong under Part XI of the Companies Ordinance as a non-Hong Kong company on 2 March 2011. In compliance with the requirements of the Companies Ordinance, Ms. Liu Li, an executive Director, of the Company, has been appointed as the agent of the Company for the acceptance of service of process and any notice required to be served on the Company in Hong Kong at Room 1303, 13/F., Keen Hung Commercial Building, 80 Queen's Road East, Wanchai.

As the Company was incorporated in the Cayman Islands, it operates subject to the Companies Law and its constitution, which comprises the memorandum of association and the Articles of Association. A summary of various parts of the constitution and relevant aspects of the Companies Law is set out in Appendix IV to this prospectus.

B. Changes in share capital of the Company

- (a) As at the date of incorporation of the Company, its authorised share capital was HK\$387,500 divided into 38,750,000 shares of HK\$0.01 each. On 2 February 2011, 60 subscriber's Shares were allotted and issued as fully paid to LinkBest.
- (b) On 2 February 2011, the Company allotted and issued 40 Shares to Open Venture. As a result, the Company is held as to 60% by LinkBest and 40% by Open Venture.
- (c) Pursuant to the written resolutions of the Shareholders passed on 20 October 2011, the authorised share capital of the Company was increased from HK\$387,500 to HK\$10,000,000 by the creation of an additional 961,250,000 Shares.
- (d) Pursuant to the said written resolutions of the shareholders and conditional upon the share premium account of Company being credited as a result of the issue of new Shares under the Placing, the Company will allot and issue 89,999,940 and 59,999,960 Shares to LinkBest and Open Venture, respectively, credited as fully paid, by way of a capitalisation of HK\$1,499,999 standing to the credit of the share premium account of the Company.
- (e) Immediately upon completion of the Capitalisation Issue (but taking into no account of any Shares which may be issued upon the exercise of the options that has been conditionally granted under the Pre-IPO Share Option Scheme and may be granted under the Share Option Scheme) and the Placing, 200,000,000 Shares will be issued fully paid or credited as fully paid and 800,000,000 Shares will remain unissued.
- (f) Save as disclosed herein and as mentioned in the following paragraphs respectively headed "Written resolutions of the Shareholders" and "Corporate Reorganisation", there has been no alteration in the share capital of the Company.

Other than pursuant to the exercise of any options which have been granted under the Pre-IPO Share Option Scheme and that may be granted under the Share Option Scheme, the Directors do not have any present intention to issue any of the authorised but unissued share capital of the Company and, without the prior approval of the Shareholders at general meeting, no issue of Shares will be made which would effectively alter the control of the Company.

C. Written resolutions of the Shareholders

Pursuant to the resolutions in writing passed by the Shareholders on 20 October 2011:

- (a) the Company approved and adopted the Articles of Association with immediate effect;
- (b) the authorised share capital of the Company was increased from HK\$387,500 to HK\$10,000,000 by the creation of an additional 961,250,000 Shares each ranking pari passu in all respects with its then existing Shares;
- (c) conditional on the Stock Exchange granting listing of, and permission to deal in, the Shares, in issue and to be issued as mentioned in this prospectus and on the obligations of the Underwriter under the Underwriting Agreement becoming unconditional and not being terminated in accordance with the terms therein or otherwise, in each case on or before the date determined in accordance with the terms of the Underwriting Agreement:–
 - (i) the Placing was approved and the Directors were authorised to approve the allotment and issue of the Placing Shares under the terms and conditions as set out in this prospectus; and
 - (ii) the rules of the Pre-IPO Share Option Scheme and the Share Option Scheme were approved and adopted and the Directors were authorised to grant options to subscribe Shares under the Pre-IPO Share Option Scheme and the Share Option Scheme and to allot, issue and deal with Shares pursuant to the exercise of options which may be granted under the Pre-IPO Share Option Scheme and the Share Option Scheme;
- (d) conditional on the share premium account of the Company being credited as a result of the Placing, the Directors be and are hereby authorised to capitalise HK\$1,499,999 standing to credit of the share premium account of the Company and to apply such sum in paying up in full at par 149,999,900 Shares for allotment and issue to holder(s) of Shares whose name(s) appear(s) on the register of members of the Company as at the close of business of the date of this resolution in proportion (or as nearly as possible without involving fractions) to their then existing shareholding in the Company;

- (e) a general unconditional mandate was given to the Directors to allot, issue and deal with, otherwise than by way of rights issue, open offer, scrip dividend or similar arrangements in accordance with the Articles, or upon the exercise of any options to be granted pursuant to the Pre-IPO Share Option Scheme and the Share Option Scheme or any other option scheme or pursuant to the Placing or the Capitalisation Issue, Shares with an aggregate nominal amount not exceeding the sum of:
- (i) 20% of the aggregate nominal amount of the share capital of the Company in issue and to be issued immediately following completion of the Placing and the Capitalisation Issue (excluding Shares which may be issued pursuant to the exercise of the options which may be granted under the Pre-IPO Share Option Scheme and the Share Option Scheme); and
 - (ii) the aggregate nominal amount of share capital of the Company which may be repurchased by the Company pursuant to the authority granted to the Directors referred to in paragraph (f) below, until the conclusion of the next annual general meeting of the Company, or the expiration of the period within which the next annual general meeting of the Company is required by any applicable law or the Articles or any applicable law to be held, or the passing of an ordinary resolution by the Shareholders in general meeting revoking, varying or renewing the authority given to the Directors, whichever occurs first; and
- (f) a general unconditional mandate was given to the Directors authorising them to exercise all powers of the Company to repurchase on GEM or any other stock exchange on which the securities of the Company may be listed and which is recognised by the SFC and the Stock Exchange for this purpose, in accordance with all applicable laws and the requirements of the GEM Listing Rules or equivalent rules or regulations of such other stock exchange, Shares with an aggregate nominal amount not exceeding 10% of the aggregate nominal amount of the share capital of the Company in issue and to be issued immediately following completion of the Placing and the Capitalisation Issue at any time until the conclusion of the next annual general meeting of the Company, or the expiration of the period within which the next annual general meeting of the Company is required by the Articles or any applicable law to be held, or the passing of an ordinary resolution by the Shareholders in general meeting revoking, varying or renewing the authority given to the Directors, whichever occurs first.

D. Corporate Reorganisation

The companies comprising the Group underwent the Reorganisation to rationalise the Group's structure in preparation for the listing of the Shares on GEM which involve the following:-

(a) Change of names to Renheng Global and Renheng Tech

To streamline the English company names within the Group, on 21 December 2010, the English name of Yanlord Global Limited was changed to Renheng Global and on 28 December 2010 the English name of Yanlord Tech Limited was changed to Renheng Tech with their respective Chinese names remain unchanged.

(b) Incorporation of BVI companies by Mr. Wei and Ms. Liu

- (i) On 1 July 2010, LinkBest was incorporated in the BVI, with an authorised share capital of US\$50,000 divided into 50,000 shares of US\$1.00 each. On 7 December 2010, LinkBest issued 100 ordinary shares, being the entire issued share capital of the company, to Mr. Wei and Mr. Wei became its sole shareholder.
- (ii) On 8 October 2010, Open Venture was incorporated in the BVI, with an authorised share capital of US\$50,000 divided into 50,000 shares of US\$1.00 each. On 7 December 2010, Open Venture issued 100 ordinary shares, being the entire issued share capital of the company, to Ms. Liu and Ms. Liu became its sole shareholder.
- (iii) On 15 December 2010, LinkBest and Open Venture, respectively entered into a sale and purchase agreement with Yanlord Industry Investment to purchase 30,000 and 20,000 issued shares of Renheng Global, being the entire issued share capital of Renheng Global. Upon completion of the sale and purchase of Renheng Global on 15 December 2010, Renheng Global was held as to 60% and 40% by LinkBest and Open Venture, respectively.

(c) Incorporation of the Company

- (i) On 2 February 2011, the Company was incorporated in the Cayman Islands with an authorised share capital of HK\$387,500 divided into 38,750,000 shares of HK\$0.01 each to act as the ultimate holding company of the Group.
- (ii) On 2 February 2011, 60 subscriber's Shares were allotted and issued as fully paid to LinkBest.

- (iii) On 2 February 2011, LinkBest and Open Venture entered into a share swap agreement with the Company (the “**Share Swap Agreement**”). Pursuant to the Share Swap Agreement, LinkBest and Open Venture transferred 30,000 and 20,000 issued shares of Renheng Global to the Company respectively by way of share swap in consideration and exchange of the Company issuing and allotting 60 and 40 Shares at par, credited as fully paid, to LinkBest and Open Venture, respectively.
- (iv) On 2 February 2011, the Company allotted and issued 40 Shares to Open Venture.
- (v) As a result of the above, a total of 60 (60%) and 40 (40%) Shares had been acquired by or issued to LinkBest and Open Venture respectively.
- (vi) Upon completion of the above, LinkBest and Open Venture became the holding companies of the Company and Renheng Global became the direct wholly-owned subsidiary of the Company.

(d) Capitalisation Issue

- (i) In order to achieve the percentage shareholding in the Company after the Listing, the Capitalisation Issue will be made, further details of which are set out under item (d) of paragraph B headed “Changes in share capital of the Company” in this Appendix.
- (ii) Upon completion of the Capitalisation Issue (but taking into no account of any Shares which may be issued upon the exercise of the options that has been granted under the Pre-IPO Share Option Scheme and may be granted under the Share Option Scheme), the Company will be held as to 45%, 30% and 25% by LinkBest, Open Venture and the public respectively.

E. Changes in share capital of subsidiaries

The Company’s subsidiaries are referred to in the Accountant’s Report of the Company, the text of which is set out in Appendix I to this prospectus. There has been no alteration in the share capital of any subsidiary of the Company within the two years preceding the date of this prospectus.

F. Repurchase by the Company of its own securities

This section includes information required by the Stock Exchange to be included in this prospectus concerning the repurchase by the Company of its own securities:

(a) Provisions of the GEM Listing Rules

The GEM Listing Rules permit companies whose primary listing is on GEM to repurchase in cash their securities on GEM subject to certain restrictions, a summary of which is set out below:

(a) Shareholders' approval

All proposed repurchases of securities, which must be fully paid up in the case of shares, on GEM by a company with its primary listing on GEM must be approved in advance by an ordinary resolution of the Shareholders, either by way of general mandate or by specific approval of a particular transaction.

Note: Pursuant to the written resolutions passed by the Shareholders on 20 October 2011, a general unconditional mandate (the "repurchase mandate") was given to the Directors authorising them to exercise all powers of the Company to repurchase its Shares on GEM, or on any other stock exchange on which the securities of the Company may be listed and which is recognised by the SFC and the Stock Exchange for this purpose, in accordance with all applicable laws and the requirements of the GEM Listing Rules or equivalent rules or regulation of other stock exchange, Shares with an aggregate nominal amount not exceeding 10% of the aggregate nominal amount of the share capital of the Company in issue and to be issued immediately following completion of the Placing and the Capitalisation Issue (excluding Shares which may be issued pursuant to the exercise of the options may be granted under the Pre-IPO Share Option Scheme and the Share Option Scheme) at any time until the conclusion of the next annual general meeting of the Company, the expiration of the period within which the next annual general meeting of the Company is required by the Articles or any applicable laws to be held or when such mandate is revoked, varied or renewed by an ordinary resolution of the shareholders of the Company in a general meeting, whichever is the earliest.

(b) Source of funds

Any repurchase by the Company may only be funded out of funds legally available for such purpose in accordance with its memorandum of association and the Articles, the applicable laws of the Cayman Islands and the GEM Listing Rules. The Company may not repurchase its own securities on GEM for a consideration other than cash or for settlement otherwise than in accordance with the trading rules of the Stock Exchange from time to time.

(c) Shares to be repurchased

The GEM Listing Rules provide that the shares which are proposed to be repurchased by a company must be fully paid up.

(b) Reasons for repurchases

The Directors believe that it is in the best interests of the Company and the Shareholders for the Directors to have a general authority from the Shareholders to enable the Company to repurchase the Shares in the market. Repurchases of the Shares will only be made when the Directors believe that such repurchases will benefit the Company and the Shareholders as a whole. Such repurchases may, depending on market conditions and funding arrangements at the time, lead to an enhancement of the net asset value per Share and/or earnings per Share.

(c) Funding of repurchases

Repurchase pursuant to the repurchase mandate would be financed out of funds of the Company legally available for such purpose in accordance with its memorandum of association and the Articles, the GEM Listing Rules and the applicable laws of the Cayman Islands. The Directors consider that, if the repurchase mandate were to be exercised in full, it might have a material adverse effect on the working capital and/or the gearing position of the Company as compared with the position disclosed in this prospectus. However, the Directors do not propose to exercise the repurchase mandate to such an extent as would, in the circumstances, have a material adverse effect on the working capital requirements of the Company or its gearing levels.

(d) Director's undertaking

The Directors have undertaken to the Stock Exchange that, they will exercise the power of the Company to repurchase the Company's securities in accordance with the GEM Listing Rules, the applicable laws and regulations of the Cayman Islands and the Articles.

(e) Disclosure of interests

None of the Directors or, to the best of their knowledge, having made all reasonable enquiries, any of their respective associates, as defined in the GEM Listing Rules, has any present intention to sell any Shares to the Company or its subsidiaries.

No connected person, as defined in the GEM Listing Rules, has notified the Company that he or she has a present intention to sell Shares to the Company, or has undertaken not to do so, if the repurchase mandate is exercised.

(f) Takeovers Code consequences

If, as a result of a securities repurchase pursuant to the repurchase mandate, a shareholder's proportionate interest in the voting rights of the Company increases, such increase will be treated as an acquisition for the purpose of The Codes on Takeovers and Mergers and Share Repurchases (the "**Takeovers Code**").

Accordingly, a shareholder, or a group of shareholders acting in concert, depending on the level of increase of shareholders' interest, could obtain or consolidate control of the company and become obliged to make a mandatory offer in accordance with Rule 26 of the Takeovers Code as a result of any such increase. Save as aforesaid, the Directors are not aware of any consequences which may arise under the Takeovers Code if the repurchase mandate is exercised.

The Directors have no present intention to exercise the repurchase mandate to such an extent as would result in takeover obligations under the Takeovers Code.

G. Particulars of Baoying Renheng

Set out below is a summary of the corporate information of Baoying Renheng:-

Company Name:	寶應仁恒實業有限公司 Bao Ying Ren Heng Industrial Co., Ltd
Date of Establishment:	1 November 2001
Registered Office:	North, Suzhong Road Baoying County Yangzhou Jiangsu Province PRC
Nature:	Limited liability company (wholly foreign owned)
Term:	Between 1 November 2001 and 31 October 2013
Registered Capital:	RMB42,857,142.86 (fully-paid up)
Registered Owner:	RENHENG Tech Limited (仁恆科技有限公司) (100%)
Legal Representative:	Sun Zhaohui

2. FURTHER INFORMATION ABOUT THE BUSINESS OF THE GROUP

A. Summary of material contracts


The following contracts (not being contracts in the ordinary course of business) have been entered into by the Company or any of its subsidiaries within the two years immediately preceding the date of this prospectus and are or may be material:

- (a) a share swap agreement dated 2 February 2011 entered into among the Company, Renheng Global, LinkBest and Open Venture, pursuant to which LinkBest and Open Venture transferred the entire issued share capital of Renheng Global in consideration of and exchange for the shares of the Company;
- (b) the Non-Competition Undertaking;
- (c) a deed of indemnity dated 20 October 2011 executed by LinkBest, Open Venture, Mr. Wei and Ms. Liu in favour of the Company containing the indemnities as referred to in “Other Information — Estate duty and tax indemnities” of this Appendix; and
- (d) the Underwriting Agreement.

B. Intellectual property rights of the Group

(a) Trade mark

The Group has registered the following trademark in Hong Kong:

Trade mark	Territory	Class	Registered Owner	Trade Mark number	Registration Date
 RENHENG Enterprise Holdings Limited 仁恒實業控股有限公司	Hong Kong	7, 11, 16, 34 and 42	the Company	301832508	14 February 2011

The trade mark registration is valid for 10 years.

The products and services covered under each registered class are set out below:-

Class No.	Specifications	Products and services of the Company
7	Machines and machine tools; motors and engines (except for land vehicles); parts of engines and motors; machine coupling and transmission components (except for land vehicles); exhausts (for vehicles); vacuum cleaners; electric drills; electric screwdrivers; incubators for eggs.	Casing and flavouring system, PF system, PP system, dedusting system, swelling agent delivery system,
11	Apparatus for lighting, heating, steam generating, cooking, refrigerating, drying, ventilating, water supply and sanitary purposes; air conditioning apparatus; electric kettles; gas and electric cookers; vehicle lights and vehicle air conditioning units.	Casing and flavouring system, PF system, dedusting system
16	Paper, cardboard and goods made from these materials; printed matter; book binding material; photographs; stationery; adhesives for stationery or household purposes; artists' materials; paint brushes; typewriters packaging materials; printers' type; printing blocks; disposable nappies of paper for babies; printed publications; paint boxes for children; cheque book holders.	Hot stamped foil
34	Tobacco; smokers' articles; matches; lighters for smokers.	Casing and flavouring system, PF system, PP system, dedusting system, swelling agent delivery system
42	Scientific and technological services and research and design relating thereto; industrial analysis and research services; design and development of computer hardware and software; computer programming; installation, maintenance and repair of computer software; computer consultancy services; design, drawing and commissioned writing for the compilation of web sites; creating, maintaining and hosting the web sites of others; design services.	Control system for casing and flavouring system, PF system, PP system, dedusting system and swelling agent delivery system and maintenance services thereof

(b) Patents

As at the Latest Practicable Date, the Group has registered the following utility and design patents in the PRC:

Utility Patent	Registered Owner(s)	Application Date	Patent number	Validity Period
氣力式柔性輸送喂絲機 (pneumatic feeding machinery)	Baoying Renheng	12-05-2006	ZL200620071271.7	11-05-2016
上吸式柔性送絲機 (updraft feeding machinery)	Baoying Renheng	27-02-2009	ZL200920036903.X	26-02-2019
帶稱重傳感器的煙用料罐 (tobacco barrel with weight sensor)	Shanghai Tobacco (Group) Co. and Baoying Renheng	27-09-2009	ZL200920210251.7	26-09-2019
料桶自動抱夾傾倒裝置 (automatic clipping and pouring device)	Baoying Renheng	28-01-2010	ZL201020104050.1	27-01-2020
糖香料液自動調製裝置 (automatic casing and flavour liquid blending device)	Baoying Renheng	19-03-2010	ZL201020134957.2	18-03-2020
立式氣動混合加香加料裝置 (vertical pneumatic spraying device)	Nanjing University of Science and Technology and Baoying Renheng	14-04-2010	ZL201020158462.3	13-04-2020
Design Patent	Registered Owner(s)	Application Date	Patent number	Validity Period
柔性喂絲機 (氣力輸送式) (feeding machinery (pneumatic mode))	Baoying Renheng	29-04-2006	ZL200630085336.9	28-04-2016

As at the Latest Practicable Date, the Group has applied for the following utility and invention patents in the PRC:

Utility Patent	Applicant(s)	Application Date	Application number
移動式全自動料液調製裝置 (movable automatic liquid blending device)	Hongyun Honghe Tobacco (Group) Co., Ltd. And Baoying Renheng	15-03-2010	ZL201020130939.7
Invention Patent	Registered Owner(s)	Application Date	Patent number
煙草專用料桶抱夾機械手 (tobacco barrel clipping mechanical hand)	Shanghai Tobacco (Group) Co. and Baoying Renheng	27-09-2009	ZL200910196600.9
自動加香供料系統 (automatic flavour spraying system)	Shanghai Tobacco (Group) Co. and Baoying Renheng	27-09-2009	ZL200910196601.3
煙草專用料罐自動開蓋裝置 (automatic tobacco barrel-cap opening device)	Shanghai Tobacco (Group) Co. and Baoying Renheng	27-09-2009	ZL200910196602.8
一體化下吸式柔性送絲機 (integrated downdraft feeding machinery)	Shanghai Tobacco (Group) Co. and Baoying Renheng	27-09-2009	ZL200910196603.2
全自動糖料廚房系統及其工藝 (automatic casing system and related technology)	Shanghai Tobacco (Group) Co. and Baoying Renheng	27-09-2009	ZL200910196604.7
移動式全自動料液調製裝置 (movable automatic liquid blending device)	Hongyun Honghe Tobacco (Group) Co., Ltd. and Baoying Renheng	15-03-2010	ZL201010124213.7
立式氣動混合加香加料裝置 (vertical pneumatic spraying device)	Nanjing University of Science and Technology and Baoying Renheng	14-04-2010	ZL201010146373.1

(c) *Domain names*

As at the Latest Practicable Date, the Group has registered the following domain names:

Domain name	Registration date	Expiry date	Registered owner
Renhengenterprise.com.hk	25-06-2010	07-07-2012	Renheng Tech
Renheng.com.hk	25-06-2010	07-07-2012	Renheng Tech
Renhengenterprise.com.cn	05-08-2010	05-08-2012	Baoying Renheng
Renhengenterprise.com	14-07-2010	14-07-2012	Renheng Tech

3. FURTHER INFORMATION ABOUT THE DIRECTORS, SENIOR MANAGEMENT AND STAFF

A. Disclosure of interests

(a) *Interests and short positions of Directors and chief executive in the shares, underlying shares and debentures of the Company and its associated corporations*

Immediately following completion of the Placing and the Capitalisation Issue (but taking into no account of any Shares which may be issued upon the exercise of the options that were granted under the Pre-IPO Share Option Scheme and may be granted under Share Option Scheme and which may fall to be allotted and issued or repurchased by the Company pursuant to the mandates as referred to in “Further information about the Company and its subsidiaries” of this Appendix), the interests and short positions of the Directors and chief executive of the Company in the Shares, underlying Shares and debentures of the Company or its associated corporations (within the meaning of Part XV of the SFO) which, once the Shares are listed, will have to be notified to the Company and the Stock Exchange under Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have under such provisions of the SFO) or which will be required, pursuant to section 352 of the SFO, to be entered in the register as referred to therein, or pursuant to Rules 5.46 to 5.67 of the GEM Listing

Rules relating to securities transactions by the Directors to be notified to the Company and the Stock Exchange, will be as follows:

Long position in Shares

Name of Director	Capacity/ Nature of Interest	Number of Shares/ Options	Approximate percentage of shareholding interests
Mr. Wei (note 1)	Interest of a controlled corporation and family interest	150,000,000 Shares	75%
Ms. Liu (note 2)	Interest of a controlled corporation and family interest	150,000,000 Shares	75%
Mr. Sun Zhaohui (note 3)	Personal interest	200,000 Options	0.1%

Notes:

- (1) Mr. Wei is the sole shareholder of LinkBest which is interested in 90,000,000 Shares and as the spouse of Ms. Liu, he is deemed to be interested in 60,000,000 Shares held by Open Venture, being a corporation wholly owned by Ms. Liu.
- (2) Ms. Liu is the sole shareholder of Open Venture which is interested in 60,000,000 Shares and as the spouse of Mr. Wei, she is deemed to be interested in 90,000,000 Shares held by LinkBest, being a corporation wholly owned by Mr. Wei.
- (3) Mr. Sun Zhaohui, an executive Director of the Company is interested in 200,000 options granted under the Pre-IPO Share Option Scheme.

(b) *Interests and short positions of Substantial Shareholders in the shares, underlying shares and debentures of the Company and its associated corporations*

Immediately following completion of the Placing and the Capitalisation Issue (but taking into no account of any Shares which may be issued upon the exercise of the options that were granted under the Pre-IPO Share Option Scheme and may be granted under the Share Option Scheme and which may fall to be allotted or issued or repurchased by the Company pursuant to the mandates referred to in “Further Information about the Company and its subsidiaries” in this Appendix), so far as it is known to the Directors, the following persons, not being a Director or chief executive of the Company, will have an interest or short position in the Shares and underlying Shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or, who is interested, directly or indirectly, in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any member of the Group:

Long position in Shares

Name	Capacity	Number of Shares	Approximate percentage of interests
LinkBest (<i>note 1</i>)	Beneficial interest	90,000,000	45%
Open Venture (<i>note 2</i>)	Beneficial interest	60,000,000	30%

Notes:

- (1) LinkBest is wholly owned by Mr. Wei who is the spouse of Ms. Liu.
- (2) Open Venture is wholly owned by Ms. Liu who is the spouse of Mr. Wei.

(c) Particulars of service contracts

Each of the executive Directors has entered into a service agreement with the Company. The terms and conditions of each of such service agreements are similar in all material aspects and are briefly described as follows:

- (i) Each service contract is for an initial term of three years commencing on 20 October 2011. Each of these service contracts may be terminated by either party thereto giving to the other not less than three months' prior notice in writing.
- (ii) The annual remuneration (including director's fee, basic salary, allowance, non-cash benefit and retirement scheme contribution) payable from the Listing Date to Mr. Wei, Ms. Liu and Mr. Sun Zhaohui under their respective service agreements shall be approximately HK\$120,000, HK\$120,000 and HK\$540,000 respectively.
- (iii) For each completed year of service, each of the executive Directors is entitled to a management bonus, the amount of which is determined with reference to the operating results of the Group, their respective responsibilities and the performance of the executive Director.
- (iv) Each of the executive Directors shall abstain from voting and not be counted in the quorum in respect of any resolution of the Board regarding the amount of annual remuneration and management bonus payable to himself/herself.

Each of the independent non-executive Directors has entered into a letter of appointment with the Company under which each of them agreed to act as independent non-executive Director for a period of three years, commencing on 20 October 2011, unless terminated in accordance with the terms and conditions specified therein. The annual director's fee payable from the Listing Date to each of the independent non-executive Directors shall be HK\$120,000. Save for the annual director's fees mentioned above, none of the independent non-executive Directors is expected to receive any other remuneration for holding his office as an independent non-executive Director.

Save as disclosed above, none of the Directors has or is proposed to have any service agreement with the Company or any of its subsidiaries (other than contracts expiring or determinable by the employer within one year without payment of compensation other than statutory compensation).

(d) Remuneration of Directors

The Company's policies concerning remuneration of the executive Directors and the non-executive Directors are as follows:

- (i) the amount of remuneration is determined by the Remuneration Committee and on the basis of the relevant Director's experience, responsibility, qualification and competence displayed;
- (ii) non-cash benefits may be provided to the executive Directors and non-executive Directors under their remuneration package; and
- (iii) the Directors are eligible to be granted options pursuant to the Share Option Scheme, as part of their remuneration package.

During the Track Record Period, no emolument was paid (including director's fee, basic salary, allowance, non-cash benefit and retirement scheme contribution) by the Group to the Directors. Further information in respect of the Directors' remuneration is set out in Appendix I to this prospectus.

It is expected that an aggregate of approximately HK\$142,500 will be paid as remuneration to the Directors by the Group in respect of the financial year ending 31 December 2011 pursuant to the present arrangement.

Save as disclosed in Appendix I to this prospectus, none of the Directors received any remuneration or benefits in kind from the Group during the Track Record Period.

(e) Disclaimers

Save as disclosed in this prospectus:

- (i) so far as the Directors are aware, none of the Directors or chief executive of the Company has any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations, within the meaning of Part XV of the SFO, which will have to be notified to the Company and the Stock Exchange under Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which he will be taken or deemed to have under the SFO) once the Shares are listed, or which will be required, pursuant to section 352 of the SFO, to be entered in the register

referred to therein once the Shares are listed, or which will be required, pursuant to Rules 5.46 to 5.68 of the GEM Listing Rules relating to securities transactions by the Directors to be notified to the Company and the Stock Exchange, once the Shares are listed;

- (ii) so far as the Directors are aware, none of the Directors and experts referred to under the heading “Consents of experts” of this Appendix has any direct or indirect interest in the promotion of the Company, or in any assets which have within the two (2) years immediately preceding the date of this prospectus been acquired or disposed of by or leased to any member of the Group, or are proposed to be acquired or disposed of by or leased to any member of the Group;
- (iii) none of the Directors and experts referred to under the heading “Consents of experts” in this Appendix is materially interested in any contract or arrangement subsisting at the date of this prospectus which is significant in relation to the business of the Group taken as a whole;
- (iv) none of the Directors has any existing or proposed service contracts with any member of the Group, excluding contracts which are determinable by the employer within one year without payment of compensation other than statutory compensation;
- (v) the Directors are not aware of any person, not being a Director or chief executive of the Company, who will, immediately following completion of the Placing and the Capitalisation Issue, be interested in or has short positions in the Shares or underlying shares of the Company which have to be notified to the Company and the Stock Exchange under Divisions 2 and 3 of Part XV of the SFO once the Shares are listed, or, who is, directly or indirectly, interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any other member of the Group; and
- (vi) none of the experts referred to under the heading “Consents of experts” of this Appendix has any shareholding in any member of the Group or the right, whether legally enforceable or not, to subscribe for or to nominate persons to subscribe for securities in any member of the Group.

(f) Agency fees or commissions received

Information on the agency fees or commissions received by the Underwriter is set out in “Underwriting” of this prospectus.

(g) Related party transactions

During the Track Record Period, the Group was engaged in related party transactions as described in the Accountants’ Report set out in Appendix I to this prospectus and “Connected transactions” of this prospectus.

4. PRE-IPO SHARE OPTION SCHEME

A. Summary of Terms

The purpose of the Pre-IPO Share Option Scheme is to give the Directors, senior management, consultants and other employees an opportunity to have a personal stake in the Company in order to motivate them to optimise their performance and efficiency, to reward them for their past contributions, and also to retain or otherwise maintain on-going relationships with them whose contributions are important to the long-term growth and profitability of the Group. The principal terms of the Pre-IPO Share Option Scheme, approved by a written resolution of the Shareholders dated 20 October 2011, are substantially the same as the terms of the Share Option Scheme except that:

- (a) the subscription price per Share for all options granted under the Pre-IPO Share Option Scheme is 80% of the Placing Price;
- (b) the total number of Shares which may be issued upon the exercise of all options granted under the Pre-IPO Share Option Scheme is 1,300,000 Shares, representing 0.65% of the enlarged share capital of the Company immediately following completion of the Placing;
- (c) save for the options which have been granted as of the Latest Practicable Date, no further options will be granted under the Pre-IPO Share Option Scheme on or after the Listing Date; and
- (d) the option shall only be exercisable on or after 1 January 2013 and expire not later than 10 years from the date of grant.

Application has been made to the Stock Exchange for approval of the listing of, and permission to deal in, the 1,300,000 Shares to be issued pursuant to the exercise of the options granted under the Pre-IPO Share Option Scheme.

B. Outstanding options granted

As of the date of this prospectus, options to subscribe for an aggregate of 1,300,000 Shares at an exercise price of 80% of the Placing Price have been conditionally granted by the Company under the Pre-IPO Share Option Scheme. All the options under the Pre-IPO Share Option Scheme were granted on 20 October 2011 (“Pre-IPO Share Options”) and no further options will be granted under the Pre-IPO Share Option Scheme prior to the Listing Date. HK\$10.00 was payable by each grantee to the Company as consideration for grant of the options.

The options have been granted based on the performance of the grantees who have made important contributions and are important to the long term growth and profitability of the Group. A total of 10 participants including 1 executive Director, 4 members of the senior management of the Group (set out in the section headed “Directors, senior management and staff” in this prospectus) and 5 employees of the Group have been granted options under the Pre-IPO Share Option Scheme.

A summary of the grantees who have been granted options under the Pre-IPO Share Option Scheme is set out below.

Grantee	Position	Address	Number of shares to be issued upon full exercise of the Pre-IPO Share Options	Percentage of enlarged issue share capital of the Company after full exercise of the Pre-IPO Share Options
Sun Zhaohui	Executive Director	Apt Blk 116, Bukit Batok West Avenue 6, #12-230, Singapore 650116	200,000	0.10
Xu Jiagui	General manager of Baoying Renheng	Room 303, Block 3, Feng Ju Yuan, Shi Ji Yuan Xiao Qu, Bai Tian Zhong Road, Baoying County, Jiangsu Province, The PRC	200,000	0.10
Chu Kin Men	Assistant to chairman of the Company	28/F., Flat D, Block 5, Pokfulam Gardens, Pokfulam, Hong Kong	200,000	0.10
Liu Yang	Vice general manager of Baoying Renheng	Room 1001, Block 93, Hua Fa New City, No. 1 Zhuhai Da Road, Zhuhai, Guangdong, The PRC	100,000	0.05

Grantee	Position	Address	Number of shares to be issued upon full exercise of the Pre-IPO Share Options	Percentage of enlarged issue share capital of the Company after full exercise of the Pre-IPO Share Options
Su Po	Director of Baoying Renheng	Room 01, Block 9, Heng Tai Shan Zhuang, 113 Cui Jing Road, Xiang Zhou District, Zhuhai, Guangdong, The PRC	100,000	0.05
Xiao Hua Liu	Director of Baoying Renheng	Room 606, Flat 3, Block 26, No. 118 Xiang Zhou Xiang Xi Road, Xiang Zhou District, Zhuhai, Guangdong, The PRC	100,000	0.05
An Zhanqi	Chief engineer of Baoying Renheng	Room 204, Flat 1, Block 4, No. 118 Xiang Zhou Xiang Xi Road, Xiang Zhou District, Zhuhai, Guangdong, The PRC	100,000	0.05
Jia Zhi Ping	Department head of Baoying Renheng	No.58-3, Jia Jia Xiang, Baoying Cheng District, Baoying County, Jiangsu Province, The PRC	100,000	0.05
Zeng Hai Dong	Department head of Baoying Renheng	No. 18, An Xuan North Road, Baoying County, Jiangsu Province, The PRC	100,000	0.05
Ho Pui Lam Joseph	Company secretary of the Company	Flat D, 5/F., Ka On Building, 27-29 Poplar Street, Sham Shui Po, Hong Kong	100,000	0.05
Total:			1,300,000	0.65%

The options issued under the Pre-IPO Share Option Scheme represent 0.65% of the Company's enlarged issued share capital as of the Listing Date. As no options granted under the Pre-IPO Share Option Scheme can be exercised before 1 January 2013, there will not be any dilutive effect on shareholding structure or impact on earnings per Share due to the exercise of such options for the years ending 31 December 2011 and 2012. In addition, as the options are exercisable on or after 1 January 2013 and expire not later than 10 years from the date of grant, any such dilution and impact on earnings per Share will be staggered over several years. No further options will be granted under the Pre-IPO Share Option Scheme after the Listing Date.

5. SHARE OPTION SCHEME

A. Summary of terms of the Share Option Scheme

The purpose of the Share Option Scheme is to provide the people and the parties working for the interests of the Group with an opportunity to obtain an equity interest in the Company, thus linking their interest with the interests of the Group and thereby providing them with an incentive to work better for the interests of the Group.

The following is a summary of the principal terms of the Share Option Scheme conditionally approved by the written resolutions of the Shareholders passed on 20 October 2011:

(a) *Who may join*

The Board may, at its absolute discretion, offer to any (i) full-time or part-time employees of the Group; (ii) directors (including any executive, non-executive and independent non-executive Directors (where applicable)) of the Group; (iii) substantial shareholders of each member of the Group; and (iv) associates of Directors or substantial shareholders of each member of the Group; (together, the "Participants" and each, a "Participant") options to subscribe for such number of Shares as the Board may determine at a subscription price determined in accordance with sub-paragraph (c) headed "Price for Shares" below, and subject to the other terms of the Share Option Scheme summarised below.

Upon acceptance of the offer, the grantee shall pay HK\$10.00, the offered price, to the Company by way of consideration for the grant and the option shall be deemed to have been granted and to have taken effect with retrospective effect from the date on which the option is offered.

(b) *Grant of options to connected persons or any of their associates*

Any grant of options to a Participant who is a Director, chief executive, or substantial Shareholder (as defined in the GEM Listing Rules) of the Company or any of his/her/its respective associates must be approved by the independent non-executive Directors, excluding any independent non-executive Director who is a grantee of the options.

Where the Board proposes to grant any option to a Participant who is a substantial Shareholder (as defined in the GEM Listing Rules) of the Company or an independent non-executive Director, or any of his/her/its associates, and such option which if exercised in full, would result in the Shares issued and to be issued upon exercise of all options granted and to be granted pursuant to the Share Option Scheme and other share option schemes of the Company (including options exercised, cancelled and outstanding) to such Participant in the 12-month period up to and including the date of grant being proposed by the Board (the “**Relevant Date**”):

- (i) representing in aggregate more than 0.1% of the total number of Shares in issue at the Relevant Date; and
- (ii) having an aggregate value, based on the closing price of the Shares as stated in the Stock Exchange’s daily quotations sheet on the Relevant Date and if the Relevant Date is not a business day, the business day immediately preceding the Relevant Date, in excess of HK\$5 million.

Such proposed grant of options and any proposed change in the terms of options granted to a grantee who is a substantial Shareholder or an independent non-executive Director of the Company shall be approved by the Shareholders by way of a poll in general meeting and the Company shall send a circular to the Shareholders, containing all such information as may be required by the GEM Listing Rules. All the Participants concerned and all other connected persons of the Company must abstain from voting in favour of the resolution at such general meeting.

The abovementioned circular must contain the following information:–

- (a) details of the number and terms (including the subscription price) of the options to be granted to each Participant, which must be fixed before the Shareholders’ meeting and the date of the board meeting for proposing such further grant should be taken as the date of grant for the purpose of calculating the subscription price;
- (b) a recommendation from the independent non-executive Directors (excluding the independent non-executive Director who is the grantee of the options) to the independent Shareholders as to voting; and
- (c) the information required under Rules 23.02(2)(c) and (d) of the GEM Listing Rules, the disclaimer required under Rule 23.02(4) of the GEM Listing Rules and the information required under Rule 2.28 of the GEM Listing Rules.

(c) *Price for Shares*

The subscription price for the Shares under the Share Option Scheme shall be determined by the Board in its absolute discretion and notified to a Participant, provided that such price shall be at least the highest of (i) the closing price of Shares as stated in the Stock Exchange's daily quotations sheet on the date of offer of an option which must be a business day; (ii) the average closing price of the Shares as stated in the Stock Exchange's daily quotations sheet for the five consecutive business days immediately preceding the date of offer (provided that the new issue price for the listing of the Shares shall be used as the closing price for any business day falling within the period before listing of the Shares if the Shares have been listed for less than five business days before the date of offer); and (iii) the nominal value of the Share.

(d) *Maximum number of Shares*

- (i) The total number of Shares which may be allotted and issued upon the exercise of all options (excluding, for this purpose, options which have lapsed in accordance with the terms of the Pre-IPO Share Option Scheme, the Share Option Scheme and any other share option scheme(s) of the Company) to be granted under the Share Option Scheme and any other share option scheme(s) of the Company must not in aggregate exceed 20,000,000 Shares, representing 10% of the Shares in issue immediately upon completion of the Placing and the Capitalisation Issue (the "**Scheme Mandate Limit**"), unless the Company obtains a fresh approval from its Shareholders pursuant to sub-paragraph (ii) below or the options are granted pursuant to sub-paragraph (iii) below.
- (ii) The Company may seek approval of its Shareholders in general meeting to renew the Scheme Mandate Limit provided that the total number of Shares in respect of which options may be granted under the Share Option Scheme and any other share option schemes of the Company shall not exceed 10% (the "**Renewal Limit**") of the issued share capital of the Company at the date of approval to renew such limit. Options previously granted under the Pre-IPO Share Option Scheme and the Share Option Scheme (including those outstanding, cancelled, lapsed in accordance with the Share Option Scheme or exercised options) shall not be counted for the purpose of calculating the Renewal Limit. The Company shall send a circular to Shareholders containing the information and disclaimer required under the GEM Listing Rules for the purpose of seeking the approval of its Shareholders for the Renewal Limit.
- (iii) The Company may authorise the Directors to grant options to specified Participant(s) beyond the Scheme Mandate Limit or Renewal Limit if the grant of such options is specifically approved by the Shareholders in general meeting. In such case, the Company shall send a circular to Shareholders in connection with the general meeting at which their approval will be sought containing a generic description of the specified Participants who may be

granted such options, the number and terms of the option to be granted, the purpose of granting options to the specified Participants with an explanation as to how the terms of the options serve such purpose, the information and the disclaimer required under the GEM Listing Rules and such further information as may be required by the Stock Exchange from time to time.

- (iv) Notwithstanding the above, the maximum number of Shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the Pre-IPO Share Option Scheme, the Share Option Scheme and any other share option schemes of the Company must not exceed 10% of the total number of Shares in issue from time to time. No option may be granted under the Share Option Scheme or any other share option schemes if this will result in the said limit being exceeded.

The maximum number of Shares issued and to be issued upon exercise of the options granted and to be granted pursuant to the Share Option Scheme and any other share option schemes of the Group to each Participant (including both exercised and outstanding options) in any 12-month period up to and including the date of grant of the options must not exceed 1% of the total number of Shares in issue (the “**Individual Limit**”). Any further grant of options in excess of the Individual Limit in any 12-month period up to and including the date of such further grant must be subject to the approval of the Shareholders in general meeting at which such Participant and his associates must abstain from voting.

(e) Time of and restrictions on exercise of option

An option may be exercised in whole or in part in accordance with the terms of the Share Option Scheme at any time during a period to be notified by the Board to each grantee provided that the period within which the Shares may be taken up under the option must not be more than 10 years from the date of offer of the option.

There is no general requirement on the minimum period for which an option must be held or the performance targets which must be achieved before an option can be exercised under the terms of the Share Option Scheme.

(f) Rights are personal to grantee

Options granted under the Share Option Scheme must be personal to the grantee, which may not be sold, transferred, charged, mortgaged, encumbered, assigned or created any interest (whether legal or beneficial) by the grantee to or in favour of any third party over or in relation to any option.

(g) *Termination of employment*

In the event that the grantee ceases to be a Participant for any reason (other than on his death) including the termination of employment or engagement on one or more of the grounds specified in sub-paragraph (o)(vi) below, the option granted to such grantee will lapse on the date of such cessation (to the extent not already exercised) and will not be exercisable unless the Board otherwise determines to grant an extension at the absolute discretion of the Board in which event the grantee may exercise the option within such period of extension and up to a maximum entitlement directed at the absolute discretion of the Board on the date of grant of extension (to the extent which has become exercisable and not already exercised) and subject to any other terms and conditions decided at the discretion of the Board. For the avoidance of doubt, such period of extension (if any) shall be granted within and in any event ended before the expiration of the period of one month following the date of his cessation to be a Participant or the relevant option period, whichever is earlier.

(h) *Rights on cessation of employment by death*

If the grantee of an option who is an individual dies before exercising the option in full and none of the event sets out in sub-paragraph (o)(vi) below arises, his/her personal representative(s) may exercise the option up to the entitlement of the grantee as at the date of death (to the extent they have become exercisable and not already exercised) within a period of 12 months or such longer period as the Board may at its absolute discretion determine from the date of death (provided that such exercise is during the relevant option period).

(i) *Effects of alterations to share capital*

In the event of capitalisation issue, rights issue, open offer, sub-division or consolidation of the Shares, or reduction of capital in the Company whilst any option remains exercisable (excluding any alteration in the capital structure of the Company as a result of an issue of Shares as consideration in respect of a transaction to which the Company is a party), or in the event of any distribution of the Company's capital assets to its Shareholders on a pro rata basis (whether in cash or in specie) other than dividend paid out of the net profit attributable to its Shareholders for each financial year of the Company, such corresponding alterations (if any) shall be made to the number or nominal amount of Shares subject to the option so far as unexercised or the subscription price for the Shares subject to the option so far as unexercised, or any combination thereof, as an independent financial adviser appointed by the Company or the auditors for the time being of the Company shall certify in writing to the Directors, either generally or as regards any particular grantee, to be in their opinion fair and reasonable. The capacity of the independent financial adviser or the auditors in this paragraph is that of experts and not of arbitrators and their certification shall, in the absence of manifest error, be final, conclusive and binding on the Company and the grantees. The costs of the independent financial adviser or the auditors shall be borne by the Company. Notice of such alteration(s) (if any) shall be given to the grantees by the Company. Any such alteration will be made

on the basis that a Participant shall have the same proportion of the issued share capital of the Company (as interpreted in accordance with the supplementary guidance on GEM Listing Rule 23.03(13) and the note immediately after the Listing Rule (“**Supplementary Guidance**”). No such alteration will be made the effect of which would be to enable a Share to be issued at less than its nominal value. In addition, any adjustment to be made will comply with the GEM Listing Rules, the Supplemental Guidance and any future interpretation of the GEM Listing Rules issued by the Stock Exchange from time to time.

(j) Rights on a take-over or share repurchase

If a general or partial offer, whether by way of take-over or share repurchase offer (but other than by way of scheme of arrangement), is made to all the Shareholders (or all such holders other than the offeror and/or any person controlled by the offeror and/or any person acting in association or concert with the offeror) and if such offer becomes or is declared unconditional prior to the expiry of the relevant option period, the grantee (or his personal representative(s)) shall be entitled to exercise the option in full (to the extent which has become exercisable on the date of the notice of the offeror and not already exercised) at any time within one month after the date on which the offer becomes or is declared unconditional.

(k) Rights on winding up

If a notice is given by the Company to its members to convene a general meeting for the purpose of considering and, if thought fit, approving a resolution to voluntarily wind up the Company, the Company shall forthwith after it despatches such notice to each of its members give notice thereof to the grantees (or his/her personal representative(s)), who may, subject to the provisions of all applicable laws, by notice in writing to the Company (such notice to be received by the Company not later than two business days prior to the proposed general meeting) accompanied by a remittance for the full amount of the subscription price for the Shares in respect of which the notice is given, exercise the option (to the extent they have become exercisable and not already exercised) either to its full extent or to the extent specified in such notice and the Company shall, as soon as possible and in any event no later than the business day immediately prior to the date of the proposed general meeting referred to above, allot and issue such number of Shares to the grantee which falls to be issued on such exercise, credited as fully paid and register the grantee as holder thereof.

(l) Rights on a scheme of arrangement

If a general or partial offer by way of a scheme of arrangement is made to all Shareholders and has been approved by the necessary number of Shareholders at the requisite meetings, the grantee (or his personal representative(s)) may thereafter (but only until such time as shall be notified by the Company, after which it shall lapse) exercise the option (to the extent which has become exercisable and not already exercised) to its full extent or to the extent specified in the notice.

(m) Rights on compromise or arrangement

Other than a general offer or partial offer or a scheme of arrangement contemplated in sub-paragraph (l) above, if a compromise or arrangement between the Company and its members or creditors is proposed for the purposes of or in connection with the reconstruction of the Company or its amalgamation with any other company or companies, the Company shall give notice thereof to all grantees (or to their personal representatives) on the same day as it gives notice to the members or creditors of the Company summoning a meeting to consider such a compromise or arrangement, and the grantee (or his/her personal representative(s)) may, by notice in writing to the Company accompanied by the remittance for the full amount of the aggregate subscription price for the Shares in respect of which the notice is given (such notice to be received by the Company not later than two business days prior to the proposed meeting), exercise his/her option (to the extent which has become exercisable and not already exercised) either to its full extent or to the extent specified in such notice, but the exercise of an option as aforesaid shall be conditional upon such compromise or arrangement being sanctioned by the court of competent jurisdiction and becoming effective. The Company shall as soon as possible and in any event no later than the business day immediately prior to the date of the proposed meeting referred to above, allot and issue such number of Shares to the grantee which falls to be issued on such exercise credited as fully paid and register the grantee as holder of such Shares. Upon such compromise or arrangement becoming effective, all options shall lapse except insofar as previously exercised under the Pre-IPO Share Option Scheme and the Share Option Scheme. The Company may require the grantee (or his personal representative(s)) to transfer or otherwise deal with the Shares issued as a result of the exercise of options in these circumstances so as to place the grantee in the same position as nearly as would have been the case had such Shares been subject to such compromise or arrangement.

(n) Ranking of Shares

The Shares to be allotted and issued upon the exercise of an option will be subject to all the provisions of the Articles for the time being in force and will rank *pari passu* in all respects with the fully paid Shares in issue on the date of their allotment and issue (the “**Exercise Date**”) and accordingly will entitle the Shareholders to participate in all dividends or other distributions declared paid or made on or after the Exercise Date other than any dividend or other distribution previously declared or recommended or resolved to be paid or made if the record date therefor is before the Exercise Date. Shares allotted and issued upon the exercise of an option shall not carry voting rights until the name of the grantee has been duly entered into the register of members of the Company as the holder thereof.

(o) *Lapse of option*

The right to exercise an option shall lapse automatically and not be exercisable (to the extent not already exercised) on the earliest of:

- (i) the expiry of the option period;
- (ii) the expiry of the periods referred to in sub-paragraphs (g), (h) or (m), where applicable;
- (iii) subject to the court of competent jurisdiction not making an order prohibiting the offeror from acquiring the remaining shares in the offer, the expiry of the period referred to in sub-paragraph (j);
- (iv) subject to the scheme of arrangement becoming effective, the expiry of the period referred to in sub-paragraph (l);
- (v) subject to the expiry of the period of extension (if any) referred to in sub-paragraph (g), the date on which the grantee ceases to be a Participant for any reason other than his death or the termination of his employment or engagement on one or more grounds specified in (vi) below. A transfer of employment from one company in the Group to another company in the Group shall not be considered as a cessation of employment;
- (vi) the date on which the grantee ceases to be a Participant by reason of the termination of his employment on the grounds that he has been guilty of misconduct, or has been in breach of a material term of the relevant employment contract, or appears either to be unable to pay or have no reasonable prospect to be able to pay debts, or has committed any act of bankruptcy, or has become insolvent, or has been served a petition for bankruptcy or winding-up, or has made any arrangements or composition with his creditors generally, or has been convicted of any criminal offence or (if so determined by the Board, the board of the relevant subsidiary or the board of the relevant associated company of the Company, as the case may be) on any other ground on which an employer would be entitled to summarily terminate his employment at common law or pursuant to any applicable laws or under the grantee's service contract with the Company, the relevant subsidiary or the relevant associated company of the Company (as the case may be). A resolution of the Board, the board of the relevant subsidiary or the board of the relevant associated company of the Company (as the case may be) to the effect that the employment or engagement of a grantee has or has not been terminated on one or more of the grounds specified in this paragraph (v) above shall be conclusive and binding on the grantee;

- (vii) subject to sub-paragraph (k) the date of the commencement of the winding-up of the Company;
- (viii) the date on which the grantee commits a breach of sub-paragraph (f); or
- (ix) the date on which the option is cancelled by the Board as set out in sub-paragraph (t).

(p) *Period of the Share Option Scheme*

Subject to earlier termination by Shareholders' resolution in general meeting, the Share Option Scheme shall be valid and effective for a period of 10 years commencing from the date of grant, after which period no further options will be offered or granted but the provisions of the Share Option Scheme shall remain in full force and effect in respect of all options which remain exercisable at the end of such period.

(q) *Price sensitive developments*

No grant of options shall be made after a price sensitive event has occurred or a price sensitive matter has been the subject of a decision until such price sensitive information has been announced in accordance with the requirements of the GEM Listing Rules. In particular, during the period of one month immediately preceding the earlier of:

- (i) the date of the Board meeting (as such date is first notified to the Stock Exchange in accordance with the GEM Listing Rules) for the approval of the Company's results for any year, half-year, quarterly or any other interim period (whether or not required under the GEM Listing Rules); and
- (ii) the deadline for the Company to publish an announcement of its results for any year, or half-year, quarterly or any other interim period under the GEM Listing Rules (whether or not required under the GEM Listing Rules).

and ending on the date of the results announcement, no option may be granted. Such period will cover any period of delay in the publication of a results announcement.

(r) *Alterations to the Share Option Scheme and the terms of option granted under the Share Option Scheme*

- (i) Subject to (ii) below, the terms and conditions of the Share Option Scheme may be altered by resolution of the Board from time to time except that the provisions relating to matters contained in Rule 23.03 of the GEM Listing Rules shall not be altered to extend the class of persons eligible for the grant of options or to the advantage of grantees or Participants except with the prior approval of the Shareholders in general meeting, with grantees and their associates abstaining from voting, and no such alteration shall operate

to affect adversely the terms of issue of any option granted or agreed to be granted prior to such alteration except with the consent or sanction of such majority of the grantees as would be required of the Shareholders under the Articles for the time being for a variation of the rights attached to the Shares;

- (ii) Any alterations of the terms and conditions of the Share Option Scheme, which are material or change the authority of the Board, shall be approved by the Stock Exchange and the Shareholders in general meeting, except where the alterations take effect automatically under the existing terms of the Share Option Scheme;
- (iii) The amended terms of the Share Option Scheme or the option must still comply with the relevant requirements of Chapter 23 of the GEM Listing Rules;
- (iv) Any change to the authority of the Directors or scheme administrators, if any, in relation to any alteration to the terms of the Scheme must be approved by the Shareholders in general meeting.

(s) *Termination of Share Option Scheme*

The Company by ordinary resolution in general meeting or the Board may at any time terminate the operation of the Share Option Scheme and in such event no further option shall be offered but the provisions of the Share Option Scheme shall remain in full force and effect in all other respects in respect of any options granted prior thereto but not yet exercised at the time of termination.

(t) *Cancellation of Options*

The Board may, with the consent of the relevant grantee, at any time cancel any option granted but not exercised. Where the Company cancels options and offers new options to the same option holder, the offer of such new options may only be made under the Share Option Scheme with available options (to the extent not yet granted and excluding the cancelled options) within the limit approved by the Shareholders as mentioned in sub-paragraph (d) headed "Maximum number of Shares" above.

B. Present status of the Share Option Scheme

As at the Latest Practicable Date, no option has been granted under the Share Option Scheme. Application has been made to the Stock Exchange for the granting of the listing of, and permission to deal in, the Shares which may fall to be issued pursuant to the exercise of the options under the Share Option Scheme.

6. OTHER INFORMATION

A. Estate duty and tax indemnities

Each of LinkBest, Open Venture, Mr. Wei and Ms. Liu (the “Indemnifiers”) has, pursuant to a deed of indemnity referred to in “Summary of material contracts” of this Appendix, given joint and several indemnities in favour of the Company in respect of among other things (a) any liability for Hong Kong estate duty which might be incurred by any member of the Group by virtue of any transfer of property (within the meaning of sections 35 and 43 of the Estate Duty Ordinance (Chapter 111 of the Laws of Hong Kong) or the equivalent thereof under the laws of any jurisdiction outside Hong Kong) to any member of the Group on or before the date on which the Placing becomes unconditional, and (b) any tax liabilities (including all fines, penalties, costs, charges, expenses and interest incidental or relating to taxation) which might be payable by any member of the Group in respect of any income, profits or gains earned, accrued or received or deemed to have been earned, accrued or received on or before the Listing Date whether alone or in conjunction with any other event, whenever occurring and whether or not the relevant taxation is chargeable against or attributable to any other person including any and all taxation resulting from the receipt by any member of the Group of any amount paid by the Indemnifiers under the deed of indemnity.

The Indemnifiers shall not be under any liability in respect of any taxation:

- (a) to the extent that full provision or allowance has been made for such taxation in the audited accounts of the Group for the Track Record Period, as set out in Appendix I to this prospectus;
- (b) for which any members of the Group is liable as a result of any event occurring or income or profits earned, accrued or received or alleged to have been earned, accrued or received or transactions entered into by the Indemnifiers or any members of the Group in the ordinary course of business after the Listing Date;
- (c) to the extent that such taxation arises or is incurred as a result of any change in law having retrospective effect and coming into effect after the Listing Date or to the extent that such taxation arises or is increased by an increase in rates of taxation after the Listing Date with retrospective effect;
- (d) for which any members of the Group is liable in respect of any accounting period commencing immediately after the Track Record Period unless liability for such taxation would not have arisen but for some act or omission of, or transaction entered into by, any members of the Group (whether alone or in conjunction with some other act, omission or transaction, whenever occurring) which are carried out or effected in the ordinary course of business on or before the Listing Date; or
- (e) to the extent of any provisions or reserve made for taxation in the audited accounts of the Group up to 30 June 2011 which is finally established to be an over-provision or an excessive reserve.

The Directors have been advised that no material liability for estate duty is likely to fall on any member of the Group in the Cayman Islands, Hong Kong, PRC and other jurisdictions in which the companies comprising the Group are incorporated.

B. Litigation

As at the Latest Practicable Date, no member of the Group was engaged in any litigation or arbitration of material importance and no such litigation or claim was known to the Directors or the Company to be pending or threatened by or against any member of the Group.

C. Sponsor

The Sponsor has made an application on behalf of the Company to the Stock Exchange for the listing of, and permission to deal in, the Shares in issue and Shares to be issued pursuant to the Placing (including any Shares to be issued under the Capitalisation Issue). The Sponsor is independent of the Company pursuant to Rule 6A.07 of the GEM Listing Rules.

D. Preliminary expenses

The preliminary expenses relating to the incorporation of the Company are approximately HK\$20,000 and have been paid by the Company.

E. Promoters

The Company has no promoter within the two years preceding the date of this prospectus, no amount or benefit has been paid or given to the promoter in connection with the Placing or the related transactions described in this prospectus.

F. Qualifications of experts

The following are the qualifications of the experts which have given their opinions or advice which are contained in this prospectus:

Names of expert	Qualification
Shenyin Wanguo Capital (H.K.) Limited	Licensed to conduct type 1 (dealing in securities), type 4 (advising on securities) and type 6 (advising on corporate finance) regulated activities under the SFO
Deloitte Touche Tohmatsu	Certified public accountants
Greater China Appraisal Limited	Professional property valuers
Maples and Calder	Cayman Islands legal advisers
Grandall Legal Group (Shenzhen)	Qualified PRC lawyers

G. Consents of experts

Each of Shenyin Wanguo, Deloitte Touche Tohmatsu, Greater China Appraisal Limited, Maples and Calder and Grandall Legal Group (Shenzhen) has given and has not withdrawn their respective written consents to the issuance of this prospectus with the inclusion of their reports and/or letters and/or valuation certificates and/or other references to their names, all of which are dated the date of the prospectus, in the form and context in which they respectively appear in the prospectus.

H. Binding effect

This prospectus shall have the effect, if an application is made in pursuance hereof, of rendering all persons concerned bound by all provisions (other than penal provisions) of sections 44A and 44B of the Companies Ordinance so far as applicable.

I. No material adverse change

The Directors confirm that there has been no material adverse change in the financial prospects of the Company or its subsidiaries since 30 June 2011 (being the date to which the latest audited financial statements of the Company were made up).

J. Miscellaneous

- (a) Save as disclosed in this prospectus:
- (i) within the two years preceding the date in this prospectus, no share or loan capital of the Company or any of its subsidiaries has been issued or agreed to be issued fully or partly paid either for cash or for a consideration other than cash;
 - (ii) within the two years preceding the date in this prospectus, no share or loan capital of the Company or any of its subsidiaries is under option or is agreed conditionally or unconditionally to be put under option;
 - (iii) no founders, management or deferred shares of the Company have been issued or agreed to be issued;
 - (iv) within the two years preceding the date of this prospectus, no commission, discounts, brokerages or other special terms have been granted in connection with the issue or sale of any capital of the Company;
 - (v) no outstanding convertible debt securities or debenture have been issued by the Company or any of its subsidiaries; and
 - (vi) there has not been any interruption in the business of the Group which may have or have had a significant effect on the financial position of the Group in the twenty-four (24) months preceding the date of this prospectus.

- (b) Save as disclosed in this prospectus, none of Shenyin Wanguo, Deloitte Touche Tohmatsu, Greater China Appraisal Limited, Maples and Calder and the PRC Legal Advisers or any of their respective directors, employees and associates:
 - (i) is interested legally or beneficially in any shares in any member of the Group;
or
 - (ii) has any right or option (whether legally enforceable or not) to subscribe for or nominate a person to subscribe for any shares in any member of the Group; or
 - (iii) has any direct or indirect interest in the promotion of, or in any assets which have been acquired or disposed of by or leased to the Company within the three years immediately preceding the date of this prospectus, or which are proposed to be acquired or disposed of or leased to the Company
- (c) No company within the Group is presently listed on any stock exchange or traded on any trading system.

A. DOCUMENTS DELIVERED TO THE REGISTRAR OF COMPANIES

The documents attached to the copy of this prospectus delivered to the Registrar of Companies in Hong Kong for registration were the written consents referred to in the paragraph headed “Consents of experts” of Appendix V to this prospectus, and copies of the material contracts referred to in the paragraph headed “Summary of material contracts” of Appendix V to this prospectus.

B. DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents will be available for inspection at the principal place of business of the Company at Room 1303, 13/F, Keen Hung Commercial Building, 80 Queen’s Road East, Wanchai, Hong Kong, during normal business hours up to and including the date which is 14 days from the date of this prospectus:

- (i) the memorandum of association of the Company;
- (ii) the Articles;
- (iii) the accountants’ report of the Company prepared by Deloitte Touche Tohmatsu, the text of which is set out in Appendix I to this prospectus;
- (iv) the accountants’ report prepared by Deloitte Touche Tohmatsu in respect of the unaudited pro forma financial information, the text of which is set out in Appendix II to this prospectus;
- (v) the audited consolidated financial statements of the Group for each of the two years ended 31 December 2010 and the six months ended 30 June 2011;
- (vi) the letter, summary of valuation and valuation certificate relating to the Group’s property interests prepared by Greater China Appraisal Limited, the text of which are set out in Appendix III to this prospectus;
- (vii) the letter prepared by Maples and Calder summarising certain aspects of the Cayman Islands Company Law as referred to in Appendix IV to this prospectus;
- (viii) the legal opinion prepared by Grandall Legal Group (Shenzhen) in respect of certain aspects of the Group and our property interests in the PRC;
- (ix) the service contracts referred to in the paragraph headed “Particulars of service contracts” in Appendix V to this prospectus;
- (x) the material contracts referred to in the section headed “Summary of material contracts” in Appendix V to this prospectus;

- (xi) the written consents referred to in the paragraph headed “Consents of experts” in Appendix V to this prospectus;
- (xii) the Companies Law;
- (xiii) the rules of the Pre-IPO Share Option Scheme and of the Share Option Scheme; and
- (ix) The full list of grantees under the Pre-IPO Share Option Scheme with all the particulars required under paragraph 10(d) of the Third Schedule to the Companies Ordinance and Rule 23.02(1)(b) and paragraph 27 of Appendix 1A to the GEM Listing Rules.